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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1944

No. 835

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, PETITIONERS,

vs.

THE UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED MAY 12, 1944.

CERTIORARI GRANTED JUNE 12, 1944.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 83

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, PETITIONERS,

vs.

THE UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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[fol. 1] **IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT**

UNITED STATES OF AMERICA, Plaintiff-Appellee,

vs.

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, Defendants-Appellants.

STATEMENT UNDER RULE 13

This action was commenced by the service of Summons and Bill of Complaint on or about March 23, 1938.

Issue was joined by the service of the answer of the State of New York on or about the 11th day of April, 1938, and the answer of the defendants Saratoga Spring Commission and Saratoga Springs Authority on or about April 13, 1938.

Trial was had on a stipulated statement of facts before District Judge Frederick H. Bryant without a jury on the 2nd day of April, 1942, and resulted in a decision in favor of the plaintiff against the defendants, dated May 10, 1943.

Judgment was entered May 12, 1943, and an amended judgment was entered June 3, 1943.

Appeals were taken by all of the defendants August 5, 1943.

[fol. 2] Plaintiff originally appeared by Hon. Ralph L. Emmons, United States Attorney, and now appears by Hon. Irving J. Higbee, United States Attorney.

The defendant State of New York originally appeared by Hon. John J. Bennett, Attorney General, and now appears by Hon. Nathaniel L. Goldstein, Attorney General.

The defendants Saratoga Springs Commission and Saratoga Springs Authority originally appeared by Hon. Spencer B. Eddy and now appear by Hon. Denis J. Harrington.

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF NEW YORK

No. Law 2503

UNITED STATES OF AMERICA, Plaintiff,

against

STATE OF NEW YORK, AND SARATOGA SPRINGS COMMISSION, AND SARATOGA SPRINGS AUTHORITY, Defendants.

SUMMONS

To the above-named defendants:

You are hereby summoned to answer the complaint in this action, and to serve a copy of your answer on the plaintiff's attorney within twenty days after the service of this summons, exclusive of the day of service; and in case of your failure to appear, or answer, judgment will be [fol. 3] taken against you by default for the relief demanded in the complaint.

Witness, The Honorable Frank Cooper, United States District Judge, at the City of Utica, in the Northern District of New York, this 23rd day of March, in the year of our Lord, one thousand nine hundred and thirty-eight.

G. A. Porter, Clerk. (Seal.)

Ralph L. Emmons,
Plaintiff Attorney,
Office and Post Office Address,
U. S. Attorney,
Binghamton, New York.

IN UNITED STATES DISTRICT COURT

BILL OF COMPLAINT

The plaintiff, United States of America, by its attorney, Ralph L. Emmons, United States Attorney in and for the Northern District of New York, for its complaint herein alleges as follows:

1. That at all the times hereinafter mentioned plaintiff has been and now is a corporation sovereign and body politic.

2. That the defendant, State of New York, is a corporation sovereign and body politic, engaged in the business of bottling for sale and selling in closed containers natural and artificial mineral and table waters at a price in excess of 12½ cents per gallon with its principal place of business in the County of Saratoga, State of New York, within the [fol. 4] jurisdiction of this Court, and was so engaged at the times hereinafter mentioned.

3. That the defendant, Saratoga Springs Commission, is a body corporate, organized, created, and existing under and by virtue of the laws of the State of New York and is engaged in the business of bottling for sale and selling in closed containers natural and artificial mineral and table waters at price in excess of 12½ cents per gallon with its principal office and place of business in the County of Saratoga in the State of New York, within the jurisdiction of this Court, and was so organized, created, and existing and so engaged at the times hereinafter mentioned.

4. That the defendant, Saratoga Springs Authority, is a body corporate, organized, created, and existing under and by virtue of the laws of the State of New York and is engaged in the business of bottling for sale and selling in closed containers natural and artificial mineral and table waters at a price in excess of 12½ cents per gallon with its principal office and place of business in the County of Saratoga, State of New York, within the jurisdiction of this Court, and was so organized, created and existing and so engaged at the times hereinafter mentioned.

5. That the plaintiff is in doubt as to which of the said defendants is liable to it in the premises and therefore joins all as parties to this action to the end that their several liability or liabilities may be determined.

6. That this is an action at law by the United States of a civil nature arising in connection with the administration of the laws of Congress providing for internal revenue and its institution is authorized and directed by the [fol. 5] Attorney General of the United States at the request of the Commissioner of Internal Revenue.

7. That returns disclosing the amount of tax due, if payable, on the bottling for sale and sale in closed containers of natural and artificial mineral and table waters by the

defendants during the period from June 21, 1932, to May 10, 1934, inclusive, were filed by defendants, under protest, with the Collector of Internal Revenue at Albany, New York. Photostat copies of said returns, together with statements attached thereto, respectively, are attached hereto and made a part hereof as Plaintiff's Exhibits A-1 to A-24, inclusive.

8. That the taxes in the amounts disclosed by said returns as due, if payable, filed as alleged, for each of the months from June 21, 1932, to May 10, 1934, inclusive, together with penalties and interest were assessed in the following amounts, on the following assessment lists and notices and demands were issued for payment of the said assessments on the following dates:

Year Month	Amount	Assessment List	Date of Demand
June 1932	Tax $60.87	Sept. 32 P. 770 L. O.	12/14/32
July 1932	Tax 295.04	Sept. 32 P. 770 L. I.	12/14/32
Aug. 1932	Tax 328.02	Sept. 32 P. 770 L. 2	12/14/32
Sept. 1932	Tax 193.18	Oct. 32 P. 2154 L. O.	12/14/32
	Int. 1.67	P. 2157 L. 5	12/14/32
Oct. 1932	Tax 233.28	Nov. 32 P. 2132 L. O.	12/15/32
Nov. 1932	Tax 176.42	Dec. 32 P. 2132 L. I.	1/18/33
Dec. 1932	Tax 140.23	Jan. 32 P. 2162 L. I.	2/10/33
	Int. 1.87	P. 2174 L. 2	2/10/33
Jan. 1933	Tax 176.06	Feb. 33 P. 2124—A L. O.	2/20/33
	Int. 1.76	P. 2129 L. 3	2/20/33
[fol. 6]			
Feb. 1933	Tax 58.48	Mar. 33 P. 2160 L. O.	4/24/33
	Int. .48	P. 2165 L. I.	4/24/33
Mar. 1933	Ta 136.85	Apr. 33 P. 2106—A. L. O.	6/1/33
	Int. 1.83	P. 2112 L. 7	6/1/33
Apr. 1933	Tax 169.07	May 33 P. 2128—A L. I.	6/13/33
	Int. 2.25	P. 2133 L. 8	6/13/38
May 1933	Tax 169.07	Jun. 33 P. 2123—A L. O.	1/3/37
	Pen. 42.26		
	Int. 3.38	P. 2132 L. 8	1/3/37
June 1933	Tax 149.31	July 33 P. 2132—A L. O.	1/3/37
	Int. 1.02	P. 2138 L. 8	1/3/37
July 1933	Tax 240.79	Aug. 33 P. 2135 L. O.	1/3/37
	Int. 3.21	P. 2142 L. 6	1/3/37
Aug. 1933	Tax 310.39	Sept. 33 P. 2117—A L. 5	1/3/37
	Int. 2.58	P. 2124 L. 4	1/3/37
Sept. 1933	Tax 287.78	Nov. 33 P. 2093 L. O.	1/3/37
	Int. 5.37	P. 2098 L. 9	1/3/37
Oct. 1933	Tax 155.46	Dec. 33 P. 2049—A L. O.	1/3/37
	Pen. 38.86		
	Int. 3.41	P. 2092 L. 7	1/3/37
Nov. 1933	Tax 245.01	Dec. 33 P. 2049—A L. I.	1/3/37
	Int. 3.26	P. 2092 L. 8	1/3/37
Dec. 1933	Tax 106.97	Jan. 34 P. 2110 L. O.	1/3/37
	Int. .83	P. 2116 L. 3	1/3/37
Jan. 1934	Tax 102.85	Mar. 34 Sp. P. 2000 L. 8	1/3/37
	Pen. 25.71		
	Int. 1.36		

Year Month	Amount	Assessment List	Date of Demand
Feb. 1934	Tax 57.28 Int. .19	Mar. 34 Sp. P. 2000 L. 7	1/3/37
Mar. 1934	Tax 150.42 Int. .50	Apr. 34 Sp. P. 2000 L. O.	1/3/37
Apr. 1934	Tax. 261.14 Int. 3.48	Jun. 34 Sp. P. 2000 L. O.	1/3/37
May 1934	Tax 124.34 Int. .41	Jun. 34 Sp. P. 2000 L. O.	1/3/37

[fol. 7] The assessments for each of the months from June, 1932, to September, 1933, inclusive, were made in the name of the defendant, Saratoga Springs Commission, and the assessments for each of the months from October, 1933, to May, 1934, inclusive, were made in the name of the defendant, Saratoga Springs Authority.

No part of said taxes, penalties, and interest assessed and demanded as aforesaid have been paid.

9. That by reason of the failure of the said defendants or any of them to pay any part of the said taxes, penalties, and interest assessed and demanded, as aforesaid, and after allowing all just credits and set-offs, there is now due and owing from the said defendants or from such of them as the Court may decide is or are liable to the plaintiff the said taxes, penalties, and interest in the following sums, together with interest at the lawful rate on said sums from the following dates, respectively:

On the sum of $878.28 with interest from December 14, 1932,

On the sum of $233.28 with interest from December 15, 1932,

On the sum of $176.42 with interest from January 18, 1933,

On the sum of $142.10 with interest from February 10, 1933,

On the sum of $177.82 with interest from February 20, 1933,

On the sum of $58.96 with interest from April 24, 1933,

On the sum of $138.68 with interest from June 1, 1933,

On the sum of $171.32 with interest from June 13, 1938,

On the sum of $2,496.64 with interest from January 3, 1937.

[fol. 8] Wherefore, plaintiff demands judgment against the defendants or against such of them as the Court may decide is or are liable to the plaintiff in the premises, for the said sums with interest at the lawful rate thereon, from the said dates, respectively, as set out hereinabove in paragraph 9 of this complaint, and the costs and disbursements of this action.

——— ———, United States Attorney.

Duly sworn to by Ralph L. Emmons. Jurat omitted in printing.

[fol. 9] IN UNITED STATES DISTRICT COURT

ANSWER OF DEFENDANT, STATE OF NEW YORK

The defendant State of New York, by John J. Bennett, Jr., its Attorney-General, answering the bill of complaint herein,

1. Denies each and all of the allegations contained in the paragraphs thereof numbered 2, 3 and 4 except that it admits that the defendant State of New York is a corporation sovereign and body politic, admits that the defendant Saratoga Springs Authority is a public benefit corporation created and existing under and by virtue of the laws of the State of New York, and admits that the defendant State of New York, by its agencies the Saratoga Springs Commission and Saratoga Springs Authority, did bottle for sale and sell in closed containers certain natural mineral waters at a price in excess of 12½ cents per gallon within the jurisdiction of this Court during the times alleged in said bill of complaint.

2. Admits the allegations contained in the paragraph of said bill of complaint numbered 7 except that it denies that any of the waters therein mentioned were artificial.

[fol. 10]. 3. Admits the allegation contained in the paragraph of said bill of complaint numbered 8 except that it denies that any of the assessments therein described were legally made.

4. Denies each and all of the allegations contained in the paragraph of said bill of complaint numbered 9.

The said defendant, further answering the said bill of complaint, as and for a first defense thereto, alleges that all of the waters in said bill of complaint mentioned were natural mineral waters taken from springs located upon the State reservation at Saratoga Springs, in the State of New York; that at all of the times in said bill of complaint mentioned the defendant State of New York was, and now is, the owner of the said reservation and springs and was, and now is, maintaining the same as a State health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes; that the said waters possess medicinal properties that are beneficial in the treatment of disease and are widely prescribed by physicians for that purpose; that the waters so sold were excess waters not required for use upon said reservation and were sold in their natural state; that their sale was merely incidental to the maintenance and operation of the said reservation; that all of the proceeds thereof were expended for the development and maintenance of the said reservation as a public health resort; that in the bottling and sale of the said waters the defendant State of New York was engaged in the exercise of a usual, traditional and essential governmental function; that the said waters, and their bottling and sale by the defendant State of New York, were and are immune from taxation by the plaintiff, and that the purported assessments described in said bill of complaint are invalid under [fol. 11] the Constitution of the United States and are illegal, null and void.

Wherefore, this defendant demands judgment against the plaintiff dismissing its bill of complaint, with costs.

John J. Bennett, Jr., Attorney-General of the State of New York, Attorney for Defendant State of New York, Office and Post Office Address, The Capitol, Albany, N. Y.

Duly sworn to by Wendell P. Brown. Jurat omitted in printing.

[fol. 12] In United States District Court

Answer of Defendants, Saratoga Springs Commission and Saratoga Springs Authority

The defendants Saratoga Springs Commission and Saratoga Springs Authority, by Spencer B. Eddy, their attorney, answering the bill of complaint herein,

1st. Deny each and all of the allegations contained in the paragraphs numbered 2, 3 and 4, except that they admit that the defendant State of New York is a corporation sovereign and body politic, admit that the defendant Saratoga Springs Authority is a public benefit corporation created and existing under and by virtue of the laws of the State of New York, and admit that the defendant State of New York, by its agencies the Saratoga Springs Commission and Saratoga Springs Authority, did bottle for sale and sell in closed containers certain natural mineral waters at a price in excess of 12½ cents per gallon within the jurisdiction of this Court during the times alleged in said bill of complaint.

[fol. 13] 2nd. Admit the allegations contained in the paragraph of said bill of complaint numbered 7, except that they deny that any of the waters therein mentioned were artificial.

3rd. Admit the allegations contained in the paragraph of said bill of complaint numbered 8, except that they deny that any of the assessments therein described were legally made.

4th. Deny each and all of the allegations contained in the paragraph of said bill of complaint numbered 9.

The said defendants, further answering the said bill of complaint, as and for a first defense thereto, allege that all of the waters in said bill of complaint mentioned were natural mineral waters taken from springs located upon the State reservation at Saratoga Springs, in the State of New York; that at all of the times in said bill of complaint mentioned the defendant State of New York was, and now is, the owner of the said reservation and springs and was, and now is, maintaining the same as a State health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes; that the said waters pos-

sess medicinal properties that are beneficial in the treatment of disease and are widely prescribed by physicians for that purpose; that the waters so sold were excess waters not required for use upon said reservation and were sold in their natural state; that their sale was merely incidental to the maintenance and operation of the said reservation; that all of the proceeds thereof were expended for the development and maintenance of the said reservation as a public health resort; that in the bottling and sale of the said waters the defendant State of New York was engaged in the exer- [fol. 14] cise of a usual, traditional and essential governmental function; that the said waters, and their bottling and sale by the defendant State of New York, were and are immune from taxation by the plaintiff, and that the purported assessments described in said bill of complaint are invalid under the Constitution of the United States, and are illegal, null and void.

Wherefore, these defendants demand judgment against the plaintiff dismissing its bill of complaint, with costs.

Spencer B. Eddy, Attorney for Defendants, Saratoga Springs Commission and Saratoga Springs Authority, City Hall, Saratoga Springs, N. Y.

Duly sworn to by Cyrus B. Elmore. Jurat omitted in printing.

[fol. 15] IN UNITED STATES DISTRICT COURT

STIPULATION OF FACTS

The plaintiff and the defendants herein, by their attorneys, hereby stipulate and agree that for the purposes of trial the following facts may be taken as true, subject to the right of any of the parties to object to the relevancy or materiality of the same and to introduce other and further facts not inconsistent with the facts so stipulated:

1. This is a suit by the United States, authorized and directed by the Attorney General, at the request of the Commissioner of Internal Revenue, to recover taxes, interest, and penalties assessed on the bottling for sale and sale in [fol. 16] closed containers of natural, mineral waters and table waters at a price in excess of 12½ cents per gallon by

the defendants during the period June 21, 1932, to May 10, 1934, inclusive.

2. The plaintiff and the defendant State of New York are corporations sovereign and bodies politic.

3. The defendant Saratoga Springs Commission is and at all times mentioned in the complaint was a public commission of the defendant State of New York with its powers, duties and purposes prescribed by the laws of the State of New York. The Saratoga Springs Commission, as hereinafter more fully set forth, was created by Chapter 866 of the Laws of 1930, as a temporary commission for the term of seven years, and was contained as a permanent commmission in the State Conservation Department by Chapter 279 of the Laws of 1937.

4. The defendant Saratoga Springs Authority is, and since April 18, 1933, has been a body corporate and politic constituting a public benefit corporation of defendant State of New York, with its powers, duties and purposes prescribed by the laws of the State of New York. The Saratoga Springs Authority was created by Chapter 208 of the Laws of 1933 and took over the management of the State Reservation (hereinafter more fully described) by lease from the Commission in October, 1933. It was established in order to obtain a loan from the Reconstruction Finance Corporation to aid in the further development of the Saratoga Reservation for public health purposes in accordance with the declaration contained in Chapter 866, Laws of 1930, that the development of the Saratoga Springs Reservation for public health purposes is a policy of the State.

[fol. 17] 5. The defendant Saratoga Springs Commission and the defendant Saratoga Springs Authority during the period June 21, 1932, to May 10, 1934, inclusive, bottled for sale and sold in closed containers certain natural mineral waters and natural spring water at a price in excess of 12½ cents per gallon within the jurisdiction of this Court, to vendees within and without the State of New York.

6. Returns disclosing the amount of tax payable, if due, on the sales made during the period from June 21, 1932, to May 10, 1934, inclusive, were filed by defendants, under

protest, with the Collector of Internal Revenue at Albany, New York. Said returns were filed for the months of June, 1932, to September, 1933, inclusive, by and in the name of the defendant Saratoga Springs Commission, which bottled and sold the said waters during this period, and for the months of October, 1933, to May, 1934 inclusive, by and in the name of the defendant Saratoga Springs Authority, which bottled and sold the said waters during the period last mentioned. Attached to each return was a statement as follows: "This return is filed under protest, and it is claimed by the State that no tax is due, upon the ground that the sale of the waters by the State of New York is the exercise of a governmental function."

7. The taxes in the amounts disclosed by said returns, together with interest and penalties, were assessed by the Commissioner of Internal Revenue in the following amounts on the following assessment lists and notices and demands were issued upon the proper parties for the payment of the said assessments on the following dates:

[fol. 18]

Year Month	Amount	Assessment List	Date of Demand
June 1932	Tax $60 37	Sept. 32 P. 770 L. O.	12/14/32
July 1932	Tax 295 04	Sept. 32 P. 770 L. I.	12/14/32
Aug. 1932	Tax 328 02	Sept. 32 P. 770 L. 2	12/14/32
Sept. 1932	Tax 193 18	Oct. 32 P. 2154 L. O.	12/14/32
	Int. 1 67	P. 2157 L. 5	12/14/32
Oct. 1932	Tax 233 28	Nov. 32 P. 2132 L. O.	12/15/32
Nov. 1932	Tax 176 42	Dec. 32 P. 2132 L. I.	1/18/33
Dec. 1932	Tax 140 23	Jan. 33 P. 2162 L. I.	2/10/33
	Int. 1 87	P. 2174 L. 2	2/10/33
Jan. 1933	Tax 176 06	Feb. 33 P. 2124 L. O.	2/30/33
	Int. 1 76	P. 2129 L. 3	2/20/33
Feb. 1933	Tax 58 48	Mar. 33 P. 2160 L. O.	4/24/33
	Int. 48	P. 2165 L. I.	4/34/33
Mar. 1933	Tax 136 85	Apr. 33 P. 2106—A L. O.	6/1/33
	Int. 1 83	P. 2112 L. 7	6/1/33
Apr. 1933	Tax 169 07	May 33 P. 2128—A L. I.	6/13/33
	Int. 2 25	P. 2133 L. 8	6/13/33
May 1933	Tax 169 07	Jun. 33 P. 2123—A L. O.	1/3/37
	Pen. 42 26		
	Int. 3 38	P. 2132 L. 8.	1/3/37
June 1933	Tax 149 31	July 33 P. 2132—A L. O.	1/3/37
	Int. 1 02	P. 2138 L. 8	1/3/37
July 1933	Tax 240 79	Aug. 33 P. 2135 L. O.	1/3/37
	Int. 3 21	P. 2132 L. 6	1/3/37
Aug. 1933	Tax 310 39	Sept. 33 P. 2117—A L. 5	1/2/37
	Int. 2 58	P. 2124 L. 4	1/3/37
Sept. 1933	Tax 287 78	Nov. 33 P. 2093 L. O.	1/3/37
	Int. 5 37	P. 2098 L. 9	1/3/37
Oct. 1933	Tax 155 46	Dec. 33 P. 2049—A L. O.	1/3/37
	Pen. 38 86		
	Int. 3 41	P. 2092 L. 7	1/3/37

[fol. 19]

Year Month	Amount	Assessment List	Date of Demand
Nov. 1933	Tax 245.01	Dec. 33 P. 2049—A L. 1	1/3/37
	Int. 3.26	P. 2092 L. 8	1/3/37
Dec. 1933	Tax 106.97	Jan. 34 P. 2110 L. O.	1/3/37
	Int. .83	P. 2116 L. 3	1/3/37
Jan. 1934	Tax 102.85	Mar. 34 Sp. P. 2000 L. 8	1/3/37
	Pen. 25.71		
	Int. 1.36		
Feb. 1934	Tax 57.28	Mar. 34 Sp. P. 2000 L. 7	1/3/37
	Int. .19		
Mar. 1934	Tax 150.42	Apr. 34 Sp. P. 2000 L. O.	1/3/37
	Int. .50		
Apr. 1934	Tax 261.14	Jun. 34 Sp. P. 2000 L. O.	1/3/37
	Int. 3.48		
May 1934	Tax 124.34	Jun. 34 Sp. P. 2000 L. O.	1/3/37
	Int. .41		

The assessments for each of the months from June, 1932, to September, 1933, inclusive, were made in the name of the defendant Saratoga Springs Commission, and the assessments for each of the months from October, 1933 to May, 1934, inclusive, were made in the name of the defendant Saratoga Springs Authority. No part of said taxes, interest, and penalties so assessed for which notices and demands have been so issued has been paid.

8. There exist at and in the vicinity of Saratoga Springs, in the State of New York, mineral springs characterized by a supersaturation of carbon dioxide gas, and containing in various quantities and combinations, minerals in solution, the most common of which are salt, soda, calcium, magnesium and iron in the form of chlorides and bicarbonates. These springs so existed and were known and used by the [fol. 20] Indians prior to their first use by the colonial settlers around 1775. From the time of their discovery until the present time, the waters of the various springs have been drunk and used for bathing purposes by large numbers of people. The waters of these springs have a recognized medical value, and are prescribed by physicians both for bathing and internal use.

9. From the year 1900 to the year 1912, a number of the springs was acquired and additional springs were drilled, by private companies engaged in the extraction of the natural carbonic acid gas from the waters for commercial sale. For the purpose of increasing the flow of the springs, pumps were installed by these companies with the result that immediately prior to the year 1911 no water flowed

from any of the previously flowing or spouting springs, the water level had sunk to several hundred feet below the ground and the springs were in danger of total extinction.

10. Commencing in the year 1911, for the purpose of preserving the springs and restoring them, the defendant State of New York, through various agencies, acquired all of the then existing springs, and stopped all pumping of the waters; title to all lands and springs being taken in the name of the State of New York. Title to all lands, springs and other property under the jurisdiction of the said Commission and Authority is and at all times has been in the State of New York. As a result of the measures referred to, the water levels were restored, the springs again flowed, and where permitted by the State, again spouted.

11. In 1929 the Legislature of the State of New York created a commission to investigate and report upon the [fol. 21] proper use of the State-owned springs at Saratoga Springs. Acting upon the report of that commission, the legislature by Chapter 866 of the Laws of 1930, transferred custody of the springs from the State Department of Conservation, which had had jurisdiction over them since 1916, to a newly-created agency known as the Saratoga Springs Commission. Section 1 of the act referred to declares it to be the purpose of the Legislature to develop "the Saratoga Springs Reservation as a state health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes. The development of such Reservation for public health purposes is hereby declared a policy of the state in accordance with the recommendations of the commission." By Section 4 of Chapter 866 of the Laws of 1930, the Saratoga Springs Commission was also assigned the duties and obligations previously imposed upon the State Conservation Department with reference to the Reservation at Saratoga Springs. These included the following, as stated in Section 602, Chapter 295, Laws of 1916, as amended by Section 40, Chapter 242, Laws of 1928, (New York Conservation Law, Section 653): "The Reservation property, with all the lands, springs, wells, rights and easements included therein shall forever remain and be kept, maintained and used for the purpose of restoring to their natural state and purity and preserving the said springs and wells and natural flow of water and gases therefrom; and of promoting the resort to the said

springs of the people of the state for health, and other suitable uses of the said Reservation by the people, and of identifying, safeguarding and assuring the natural purity, qualities and repute of such water and gases, and for the purpose of providing said waters to the people for drinking, free of charge."

[fol. 22] 12. At the time of the creation of the Saratoga Springs Commission, a part of the waters of the springs was, and for ten years previously had been, bottled and sold by a private corporation operating under a lease from the State of New York. One of the first actions of the Saratoga Springs Commission was to purchase from the private corporation its rights under the lease, which then had approximately 15 years to run. The purchase was effected for a sum considerably less than the anticipated profits to the bottling corporation, which was deriving a profit from its operations, during the 15 years it could legally have continued its control of the springs. Commencing May 1, 1932, the Saratoga Springs Commission took over the bottling and sale of these waters, a modern and efficient bottling works for scientific bottling of the waters having been constructed.

13. Three mineral waters and one plain water are and were during the period covered by the assessments, bottled and sold, all in their natural state. The mineral waters are Hathorn, a laxative water; Coesa, a diuretic water; and Geyser, a digestive water. These are properly classified as mineral waters; they are not suitable for indiscriminate beverage use and cannot be mixed with fruit juices or alcoholic beverages. The plain water, known as State seal, is of high chemical and vegetable purity. It is used very largely in various state institutions and offices, and a small amount is also purchased by the general public, mostly on recommendation of physicians.

14. During the period June 21, 1932, to May 10, 1934, inclusive, the Saratoga Springs Commission and Saratoga Springs Authority, as stated in the returns filed by them and referred to in paragraphs 6 and 7, above, bottled and [fol. 23] sold 216,390½ gallons of the mineral and plain waters described herein in closed containers at more than 12½¢ per gallon. Aggregate receipts from the sale of bottled waters, including a relatively small amount of plain

water sold at less than 12½¢ per gallon, were as follows for the fiscal years 1933 to 1941.:

1932-3	$104,434.98
1933-4	101,675.80
1934-5	102,275.60
1935-6	113,441.86
1936-7	138,021.40
1937-8	144,637.91
1938-9	143,611.57
1939-40	141,927.24
1940-41	135,281.33

All of the bottled waters referred to herein were sold for consumption off the Reservation. Large quantities of the above mineral waters and other mineral waters were and are consumed on the Reservation, free of charge at the springs and at various Drink Pavilions and upon payment of admission fees to the two Drink Halls, hereinafter referred to.

15. From May 1, 1932, to the present time, including the period covered by the assessments involved in this proceeding, sales of the bottled waters have been made through distributors and retailers and by direct shipments to consumers. During the period covered by the assessments the Commission and Authority, respectively, had an exclusive distributor for the Metropolitan area of New York City, including five counties in New Jersey. This distributor handled about 50% of the total waters sold at more than 12½¢ per gallon. Non-exclusive distributors were main- [fol. 24] tained in Boston, Massachusetts, Western Massachusetts, Albany, Schenectady, Troy, Buffalo, Philadelphia, Pennsylvania, Baltimore, Maryland, Washington, D. C., Chicago, Illinois and other places. This situation obtains at the present time except that the dealers in Philadelphia and Chicago have now been granted exclusive rights to the sale of the waters in their respective areas, and an exclusive dealer has been added in Miami, Florida. At all times, the dealers granted exclusive sales rights have undertaken to dispose of a fixed minimum quantity of the waters, and to do certain advertising and promotional work.

16. Advertising of the bottled waters has also been conducted during each year by the Commission and Authority,

respectively and has included space in newspapers and medical periodicals, distribution of free samples, window and counter displays and circularization. The total amounts charged to such advertising, not including advertising for the baths and other facilities, were as follows for the fiscal years 1933-41:

1932-3	$ 29,607.98
1933-4	18,392.62
1934-5	13,187.43
1935-6	3,596.06*
1936-7	24,685.39
1937-8	27,629.22
1938-9	30,925.38
1939-40	14,578.59
1940-41	17,750.89

NOTE (*) In the year 1935-6 the cost of "Free Bottled Waters" only was charged to Waters Department advertising. The total of all advertising expense for that year amounted to $72,205.92.

[fol. 25] 17. The annual report of the Commission and Authority for the year 1935-1936 contains the following paragraphs relating to publicity and advertising for both the sale of bottled waters and the services rendered at the Reservation (customarily referred to as the Saratoga Spa):

> The greatest present need is means for promotion of the Spa, not alone advertising in the customary commercial sense, but in other ways telling New Yorkers what their State has done at Saratoga to make its curative waters available for sufferers from chronic diseases. During the past five years it has been possible to spend for promotion only $150,651.17, an average of $30,130.23 per year. A comparatively small part only of this sum has been spent for advertising; all charges, whether in goods or in service that have to do with promotion being entered under this heading. It has been a wholly inadequate amount, as may be shown by comparison with the expenditures of other institutions in comparable fields.
>
> White Rock spends $400,000 a year. French [redacted] Springs spends on Pluto Water and the hotel $300,000

a year. The Greenbrier, at White Sulphur Springs, West Virginia, spent $44,215 last year, and the Homestead at Virginia Hot Springs, $30,000. One hotel at Hot Springs, Arkansas, The Arlington, spent $20,000 in advertising its baths. The Bernard McFadden "health" hotel at Dansville, N. Y., spent $90,491 last year. Foreign waters and products spend similar sums in our own market. Carlsbad products spent $80,285 last year over the radio alone in promoting the salts derived from the Czecho-Slovakian waters, with an additional $4,875 in magazine advertising. Vichy Celestin Water spent $25,000 in New York City alone.

[fol. 26] It must be borne in mind that expenditures at Saratoga have been for the Spa and its waters both, in spite of the fact that they are distinct and should be promoted individually; the Spa offering services and waters being a product. • • •

18. It has been the consistent policy of the Saratoga Springs Commission and the Saratoga Springs Authority steadily to increase the volume of waters bottled and sold and to derive the largest profit possible from this activity, in order that the proceeds might be applied to the cost of other services rendered at the Spa. In this connection, the annual report for the fiscal year 1935-36, referred to, contains the following excerpts:

We are reminded that in 1932 something happened which now threatens to change the character of the Saratoga Spa. The Legislature ceased its appropriations for a development it had authorized and for which it was expected to furnish the necessary funds. The buildings authorized were then less than half completed. In place of further appropriations the Legislature created the Saratoga Springs Authority and gave it permission to borrow from the Federal government sufficient money to finish the work. The Saratoga Springs Authority thus became responsible for repayment of a loan of $3,200,000 with interest; hence, the necessity to operate the Spa along lines yielding a profit.

Heretofore free treatments for needy and ailing citizens have been encouraged and in general the policy at

Saratoga has been to serve the public at or below cost. As a matter of fact, the number of free treatments given has grown and promises to grow as the benefits [fol. 27] of the waters become more widely known. In addition the public use of the enlarged park area is rapidly increasing the cost of its care. Also the Commission is obliged to maintain at the springs themselves a free service, for whoever may come there to drink or fill their bottles or jars. It is a conservatively estimated that this free service is enjoyed by as least 200,000 persons during the year. Another 20,000 persons—men, women and children—visit Geyser Park for recreation and picnics.

Under these circumstances the Commission seems faced with the necessity of limiting the free public function of the Spa or asking the Legislature to appropriate funds to cover the annual payments to the R. F. C. until such time as the increase of water sales turns in a sufficient profit.

The Commission fully believes that the sale of bottled waters, if properly advertised as any private corporation would advertise them, will *in the end* make such a profit and enable it to continue the policy of furnishing certain of the facilities of the Spa to the people of the State of New York free, and others at cost. Those increased water sales and profits, however, are necessarily slow of realization.

19. During the fiscal years 1933 to 1941, the following profits or losses were derived from the sales of the bottled waters, computed without depreciation or other capital charges:

1932-3	$15,368.97
1933-4	8,662.36
1934-5	12,062.79
[fol. 28] 1935-6	20,026.72
1936-7	17,050.55
1937-8	16,165.98
1938-9	7,358.24
1939-40	27,022.54
1940-41	23,249.84

All of the profits so derived, as shown by the above table, were devoted to the current expenses of other parts of the Reservation.

20. None of the watering places or spas referred to in the second paragraph of the excerpt quoted in paragraph 17 above, which are located in the United States, is owned or operated by the federal government or by any state, state commission or authority, or political subdivision. While several of these spas, as indicated, bottle and sell mineral waters to the general public, in no instance are such operations conducted by the federal government, or by any state, state commission or authority or political subdivision. The parties know of no other instance in the United States where a state, state commission or authority, or political subdivision owns and operates or either owns or operates a spa comparable in any respect to the Saratoga Spa, or of any instance where a state, state commission or authority, or political subdivision bottles or sells or either bottles or sells mineral or plain waters. The parties, likewise, know of no instance where the federal government engages in a similar activity.

21. The total available flow of the Geyser, Coesa and Hathorn No. 2 springs, from which the bottled waters are produced, is so great that the quantities of such waters consumed on the premises and the quantities bottled and [fol. 29] sold could be increased many times without injury to these or the other springs on the reservation and without deterioration of the quality of the waters.

22. Pursuant to legislative authorization, the Saratoga Springs Commission and Saratoga Springs Authority have constructed a Drink Hall, called "The Hall of Springs", Roosevelt Bath Houses Nos. 1 and 2, for administering mineral baths, an Administration and Research Laboratory Building, which includes a small theatre, a Bottling Works (referred to in paragraph 12, above), a Recreation Center, with swimming pool, golf course, outdoor gymnasium, tennis courts, and other facilities for outdoor recreation; and a building known as the Gideon Putnam Hotel-Sanitarium; and have remodeled a second Drink Hall, located in the downtown business section of Saratoga Springs. The foregoing buildings and facilities, as well as two older bath

houses, known as the Washington and Lincoln Bath Houses, and certain Drink Pavilions are located upon and are administered as a part of the State-owned Reservation or Spa. All of these buildings and facilities, except the Gideon Putnam Hotel-Sanitarium, and the theatre, were operated by the Saratoga Springs Commission during the period June, 1932, to September, 1933, inclusive, and since September, 1933, have been operated by the Saratoga Springs Authority. The Saratoga Springs Authority also operates a bus line from the City of Saratoga Springs to the Lincoln and Washington Baths, and to the Hall of Springs, Roosevelt Baths, etc., which are located about two miles south of the downtown section of Saratoga Springs. The Gideon Putnam Hotel-Sanitarium has been leased since its construction in 1933 for private operation on a [fol. 30] year-around basis and the theater was and is leased for private operation during the summer months.

23. All of the lands of the Reservation have been purchased and all improvements erected or purchased by virtue of (1) appropriations made by the Legislature of the State of New York in an aggregate amount, as of June 30, 1941, of approximately $5,620,500., and (2) a loan made by the Reconstruction Finance Corporation to the Saratoga Springs Authority in the amount of $3,200,000. It has been necessary for the Legislature of the State of New York to appropriate annually substantial sums for current operations and interest payments, in addition to the gross receipts of the Saratoga Springs Commission and Saratoga Springs Authority, respectively, which have been and are used to defray such expenses. The total annual operating receipts of the Commission and Authority have never been sufficient to meet annual expenses, exclusive of interest and amortization charges on the R. F. C. loan referred to.

24. The facilities of the Reservation are available to citizens of New York State and to the public generally on equal terms. Fees or admission prices are charged for admission to the two Drink Halls, the Bath Houses, the Recreation Center and the summer theater, except that a substantial number of charity treatments are also administered at the Bath Houses. The number of such charity treatments and their ratio to paid treatments are given in the following table, set forth in the annual report of the Saratoga Springs Commission and Saratoga Springs Authority for the fiscal year 1939-1940:

[fol. 31]

Fiscal Year	Paid Treatments	Charity Treatments	Total Treatments
1930-31	92,176	No record	92,176
1931-32	85,267	11,811	97,078
1932-33	66,343	18,755	85,098
1933-34	78,530	28,871	107,401
1934-35	81,870	15,000	98,870
1935-36	101,496	17,490	118,986
1936-37	128,334	19,217	147,551
1937-38	117,340	19,359	136,698
1938-39	111,211	24,971	136,182
1939-40	111,460	23,245	134,705
1940-41 (6 mos.)	84,708	20,041	94,749

In addition, fares are charged for transportation on the bus line. Receipts from admissions to the Bath Houses and from sales of the bottled waters have at all times constituted the two largest items of income, excepting the items of appropriations by the State Legislature to the Saratoga Springs Commission and Saratoga Springs Authority. The largest item of net income, however, has accrued from the lease of the Gideon Putnam Hotel Sanitarium.

25. All moneys of the Saratoga Commission are deposited and disbursed in accordance with Section 11 of Ch. 866 Laws of 1930.

All moneys of the Saratoga Authority are paid to the Commissioner of Taxation & Finance of the State of New York as agent of the Saratoga Springs Authority and disbursed in accordance with Section 4 of Ch. 208 L. 1933.

26. Chapter 569 Laws 1909; Chapter 394 Laws 1911, Chapter 252 Laws 1914; Chapter 866 Laws 1930; Chapter [fol. 32] 279 Laws of 1937; Chapter 208 Laws 1933 and Article XV entitled "Division of Saratoga Springs Reservation" of the Conservation Law of the State of New York are hereby referred to and made a part of this stipulation.

Executed this 6th day of October, 1941.

United States of America, by Ralph L. Emmons, United States Attorney. State of New York, by John J. Bennett, Jr., Attorney-General. Saratoga Springs Commission, Saratoga Springs Authority, by Denis J. Harrington, Their Attorney.

IN UNITED STATES DISTRICT COURT

OPINION OF BRYANT, DISTRICT JUDGE—November 17, 1942

Appearances:

Ralph L. Emmons, Esq., United States Attorney, (B. F. Tompkins, Esq., Assistant United States Attorney, Samuel O. Clark, Jr., Esq., Assistant Attorney General, Andrew D. Sharpe, Esq., and Alvin J. Rockwell, Esq., Special Assistants to the Attorney General, of Counsel,) for the plaintiff.

Hon. John J. Bennett, Jr., Attorney General of the State of New York, (Henry Epstein, Esq., Milton Kaplan, Esq., Jack Goodman, Esq., of Counsel,) for the State of New York.

[fol. 33] Messrs. Schwarte, Slade, Harrington & Goldsmith, Attorneys (John A. Slade, Esq., and Denis J. Harrington, Esq., of Counsel,) for Saratoga Springs Commission and Saratoga Springs Authority.

BRYANT, *D. J.*:

This is a suit for the collection of taxes, penalties and interest in the amount of $4,473.50, and additional interest from various dates between December 14, 1932, and January 3, 1937, inclusive, accruing under section 615 (a)(5) of the Revenue Act of 1932.

The question at issue is whether, in bottling for sale and selling certain mineral and table water, the State of New York and its agencies, Saratoga Springs Commission and Saratoga Springs Authority, are immune under the Federal Constitution from the taxes imposed by said Revenue Act. This Act imposed upon all natural or artificial mineral or table water "sold by the producer, bottler, or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of two cents per gallon."

There exists at and in the vicinity of Saratoga Springs, New York, mineral springs having a recognized medicinal value, the waters of which are prescribed by physicians both for bathing and internal use. Ever since Indian days these waters have been drunk and used for bathing purposes by vast numbers of people. Prior to the year 1912, a number of the springs had been acquired, and additional springs had been drilled, by private companies engaged

in the extraction of the natural carbonic acid gas from the waters for commercial use. In order to increase the flow of these springs, pumps had been installed. As a result of this usage, immediately prior to the year 1911, no water [fol. 34] flowed from any of the previous flowing or spouting springs; the water level had shrunk several hundred feet below the surface of the ground and the springs were in danger of total extinction. Commencing in the year 1911, the State of New York, for the purpose of restoring the springs and preserving the waters for the benefit of the people of the State and the public generally, acquired all of the then existing springs. Title to all of the lands were taken in the name of the State. These lands, and the facilities located upon them, are usually referred to as the "Saratoga Reservation."

After acquisition by the State and prior to 1930, a private corporation, operating under a lease from the State, bottled and sold mineral and table water taken from the springs.

Defendant Saratoga Springs Commission was created by Chapter 866 of the New York Laws of 1930 as a temporary commission for the term of seven years and was continued as a permanent commission in the State Conservation Department by Chapter 279 of the Laws of 1937. It is a public agency of the State of New York. Its activities and liabilities were and are those of the State. It cannot sue nor be sued in its own name. In 1930, soon after creation, it took over the custody and control of the Reservation. One of its first acts was the purchase of the private corporation's lease and its rights to bottle and sell waters. With money appropriated by the State, the Commission built a modern and efficient bottling works and on May 1st., 1932, took over the bottling and sale of the waters. It continued this activity until 1933.

In 1933, Saratoga Springs Authority came into existence under Chapter 208 of the New York Laws of 1933. It is [fol. 35] an agency of the State of New York, a public benefit corporation with its powers, duties and purposes prescribed by law. It may sue and be sued in its own name without joining the State. In 1933, soon after creation, it took over the custody, control and operation of the Reservation. Since that time, among other things, it has carried on the business of bottling and selling mineral and spring water.

The State of New York has expended, in the purchase of lands and the improvements erected thereon, in addition to $3,200,000 received as a loan from the Reconstruction Finance Corporation, approximately $5,620,500. With moneys appropriated and borrowed as above stated, the Commission and the Authority, pursuant to authorization of the New York Legislature, have constructed a drink hall, two bath houses for administering mineral baths, an Administration and Research Laboratory building which includes a small theatre, a bottling works (referred to above), a recreation center with swimming pool, golf course, outdoor gymnasium, tennis courts and other facilities for outdoor recreation and a Hotel-Sanitarium. They have also remodelled a second drink hall located in the downtown business section of the City. The foregoing buildings and facilities, as well as two older bath houses and certain drink pavilions on the premises at the time of purchase, are located upon and are administered as a part of the Reservation. All of these buildings, except the hotel-sanitarium and the theatre, were operated by the Saratoga Springs Commission during the period June, 1932, to September, 1933, inclusive, and, since the latter date, have been operated by the Saratoga Springs Authority. The Authority also operates a bus line from the City of Saratoga to the baths and springs on the Reservation. The [fol. 36] Hotel-Sanitarium has been leased, since its construction in 1935, for private operation on a year around basis and the theatre is and was leased for private operation during the summer months.

The facilities of the Reservation have at all times been available to citizens of New York State and to the public generally on equal terms. Fees are charged for admission to the two drink halls, the bath houses, the recreation center and the summer theatre, although a substantial number of charity treatments are also administered at the bath houses. In addition fares are charged for transportation on the bus line. All receipts, including the income from the lease of the hotel-sanitarium and receipts from sales of the bottled water, are used in the maintenance and upkeep of the Reservation. The gross receipts have never been sufficient to meet annual expenses, exclusive of interest and amortization charges on the loan. Annually, the Legislature of the State of New York has appropriated

substantial sums for current operations, interest charges and amortization payments.

The gross sales of bottled water amount to approximately $125,000.00 per year. The Commission and the Authority have expended something above an average of $20,000.00 per year for advertising of the bottled water. It has been, and is, the consistent policy of the Commission and the Authority steadily to increase the volume of water bottled and sold and to derive the largest profit possible from the operation. The larger the sales and the greater the profits the less deficiency there will be for the State to meet annually. [fol. 37] Upon demand the Commission and the Authority, under protest, filed with the Collector of Internal Revenue at Albany the amount of mineral and plain water bottled and sold during the period in question. The reports showed 216,890½ gallons. On the basis of these returns, taxes, penalties and interest were assessed in amounts above stated and demand for payments were made. No part of these amounts of the interest accruing thereon has been paid.

Discussion of tax immunity by virtue of the necessary implications of our dual system of government stems from McCulloch v. Maryland (4 Wheat. 316) which was the basis fifty years later of the decision in Collector v. Day (11 Wall. 113). In view of later decisions, and the review the cited decisions have had therein, consideration of these cases seems unnecessary. Plaintiff finds particular comfort, if not the whole support for its position, in Helvering v. Gerhardt, 304 U. S. 405, and the three pertinent earlier cases, which in that opinion won the express approval of the Court (South Carolina v. United States, 199 U. S. 437; Ohio v. Helvering, 292 U. S. 360; Helvering v. Powers, 293 U. S. 214), and in Allen v. Regents, 304 U. S. 439. The facts in these cases differ so materially from the facts in the case at bar that they cannot be considered direct precedents. However, the rules therein established must be followed. One is that "the immunity implied from the dual sovereignty recognized by the Constitution does not extend to business enterprises conducted by the States for gain" (Allen v. Regents, *supra*, p. 453).

Defendants argue strenuously that they are not conducting business for gain. It is their well supported contention [fol. 38] that the State of New York is engaged in a broad

program of conservation of natural resources, promotion of health and creation of recreation facilities of which the sale of bottled water is only a small part. Their argument seems to be answered by the Regents case. The State of Georgia was engaged in a governmental function, the carrying out of a program of public education. The holding of athletic contests was a fractional part of that program and yet those contests were not considered mere incidents, in the governmental program. There are marked differences of facts in the two cases. In the Regents case the tax was paid by the public. Refusal of immunity placed no burden upon the State. At most it prevented increased enrichment. Here the tax, if allowed, is a direct burden on the State. Its payment will reduce directly the revenues of the State. However, in view of the Regent case and Helvering v. Gerhardt, *supra*, it cannot be said that the business, as carried on, is free from the burden of a non-discriminating tax laid on sales.

Defendants further contend that the State of New York is engaged only in the sale of its natural resources: that under our system of dual sovereignty the United States cannot tax those resources nor the proceeds received from their sale. With the last proposition I am in accord, but I cannot accept the proposition that the State was only selling its natural resources. It took its natural resources and, through a bottling process, put those resources into a preserved condition where they could be sold to the public in competition with private waters. The bottling and sale of the waters was a business enterprise conducted for gain rather than simply a sale of the State's natural resources. Allen v. Regents, *supra*, applies.

[fol. 39] Plaintiff is entitled to judgment. For the period, June 21, 1932, to September 1933, inclusive, the waters were bottled and sold by the Saratoga Springs Commission. For the liability arising during that period, plaintiff may have judgment against the Saratoga Springs Commission and the State of New York jointly. For the liability arising during the period October, 1933, to May 10, 1934, plaintiff is entitled to judgment against the Saratoga Springs Authority.

Dated: November 17th, 1942.

Frederick H. Bryant, United States District Judge

IN UNITED STATES DISTRICT COURT

Decision—May 10, 1943

The above entitled action having been brought on for trial before this Court without a jury at a term thereof in Syracuse, New York, on the 2d day of April, 1942, upon the stipulation of facts made by the parties and filed herein, and that after hearing the evidence herein and arguments of respective counsel and consideration of the briefs filed, the Court makes the following

FINDINGS OF FACT

1. The Court finds the detailed facts in accordance with the written stipulation of the parties filed in this proceeding, to which reference is hereby made.

[fol. 40] 2. As an ultimate fact, the Court finds that in bottling for sale and selling mineral and table waters derived from the State-owned reservation at Saratoga Springs during the period June 21, 1932, to May 10, 1934, inclusive, the State of New York and its agencies, Saratoga Springs Commission and Saratoga Springs Authority embarked in a business which would normally be taxable. The activity so conducted by the State of New York and its agencies had the characteristics of a business enterprise and the waters referred to were sold in competition with private waters.

CONCLUSIONS OF LAW

1. The Court has jurisdiction of the parties and the subject matter here involved.

2. Section 615 (a) (5) of the Revenue Act of 1932 is applicable to the bottling for sale and selling of natural or artificial mineral waters or table waters when that activity is conducted by a state or its agencies.

3. No immunity from federal taxation attaches to the action of a state or its agencies in bottling for sale and selling natural or artificial mineral waters or table waters by virtue of the provisions, structure or implications of the Federal Constitution.

4. For the period June 21, 1932, to September, 1933, inclusive, plaintiff is entitled to judgment against the State

of New York and the Saratoga Springs Commission, jointly, for the taxes, penalties and interest here involved. For the period October, 1933, to May 10, 1934, inclusive, plaintiff is entitled to judgment against the Saratoga Springs Authority for the taxes, penalties and interest here involved.

[fol. 41] Judgment in accordance herewith, with costs against the State of New York and Saratoga Springs Commission, may be entered herein.

Dated: May 10, 1943.

Frederick H. Bryant, United States District Judge.

In United States District Court

Judgment—May 10, 1943

The above entitled action being at issue in this Court and brought on for trial before the Court without a jury at a term of said Court held at Syracuse, N. Y. April 3, 1942, and Ralph L. Emmons, United States Attorney for the Northern District of New York, and Alvin J. Rockwell, Attorney, U. S. Department of Justice, and B. F. Tompkins, Assistant United States Attorney, appearing for the plaintiff, and John J. Bennett, Jr. Attorney General of the State of New York, Milton J. Kaplan and Jack Goodman, Assistant Attorneys General, John A. Slade and Denis J. Harrington appearing for the defendants, Saratoga Springs Commission and Saratoga Springs Authority; and the Court having considered the arguments and briefs of counsel and the evidence and stipulation of parties filed herein, and having made and filed its findings of fact and conclusions of law thereon,

It Is Hereby Ordered, Adjudged and Decreed that the plaintiff have and recover of the defendants, the State of New York, and Saratoga Springs Commission, jointly, [fol. 42] the sum of Five Thousand Four Hundred Fifty-four Dollars and Seventy-seven Cents ($5,454,77) with interest at 52 cents per day from December 31, 1942 on $3,124.34, the tax, to date of entry hereof, and the further sum of $28.86, the costs and expenses of the plaintiff hereby taxed and allowed; and the plaintiff have and recover from the defendant, the Saratoga Springs Commission the sum of Two Thousand Eight Dollars and Forty-four Cents ($2,008.44) with interest on the tax of $1203.47 at 20 cents

per day from December 31, 1942 to date of entry of this judgment.

And that execution issue therefor.

Dated: May 10, 1943.

Frederick H. Bryant, United States District Judge.

IN UNITED STATES DISTRICT COURT

AMENDED JUDGMENT—June 1, 1943

The above entitled action being at issue in this Court and brought on for trial before the Court without a jury at a term of said Court held at Syracuse, N. Y. April 3, 1942, and Ralph L. Emmons, United States Attorney for the Northern District of New York, and Alvin J. Rockwell, Attorney, U. S. Department of Justice, and B. F. Tompkins, Assistant United States Attorney, appearing for the plaintiff, and John J. Bennett, Jr. Attorney General of the State of New York, Milton J. Kaplan and Jack Goodman, Assistant Attorneys General, John A. Slade and [fol. 42] Denis J. Harrington appearing for the defendants, Saratoga Springs Commission and Saratoga Springs Authority; and the Court having considered the agreements and briefs of counsel and the evidence and stipulation of parties filed herein, and having made and filed its findings of fact and conclusions of law thereon,

It is hereby ordered, adjudged and decreed that the plaintiff have and recover of the defendants, the State of New York, and Saratoga Springs Commission, jointly, the sum of Five Thousand Four Hundred Fifty-Four Dollars and Seventy-Seven Cents ($5,454.77) with interest at 51 cents per day from December 31, 1942 on $3,124.34, the tax, to date of entry hereof, and the further sum of $28.86, the costs and expenses of the plaintiff hereby taxed and allowed; and the plaintiff have and recover from the defendant, the Saratoga Springs Authority the sum of Two Thousand Eight Dollars and Forty-Four Cents ($2,008.44) with interest on the tax of $1203.47 at 20 cents per day from December 31, 1942 to date of entry of this judgment.

And that execution issue therefor.

The foregoing judgment is in amendment of and supersedes the judgment herein entered on May 12, 1943, and is made on stipulation of the parties interested herein.

Dated: June 1, 1943.

Frederick H. Bryant, United States District Judge.

[fol. 44] IN UNITED STATES DISTRICT COURT

STIPULATION RE JUDGMENT—June 12, 1943

It is hereby stipulated and agreed by the plaintiff that the amended judgment herein, dated May 10, 1943, and entered June 3, 1943, in which it is recited that said amended or superseding judgment "is made on stipulation of the parties interested herein" refers only to the change in the name of "Saratoga Springs Commission" to "Saratoga Springs Authority", and is not deemed or intended as meaning a consent by the defendants to entry of judgment, or to a consent judgment herein, and no such contention will be made by the plaintiff herein.

Dated: June 12, 1943.

(Sgd.) Irving J. Higbee, United States Attorney, Attorney for the Plaintiff.

IN UNITED STATES DISTRICT COURT

NOTICE OF APPEAL OF STATE OF NEW YORK—August 3, 1943

[Title omitted]

Notice is hereby given that the State of New York, one of the defendants above named, hereby appeals to the [fol. 45] Circuit Court of Appeals for the Second Circuit from so much of the judgment herein entered with the Clerk of the United States District Court for the Northern District of New York, at Utica, New York, in this action on May 12, 1943, and from so much of the amended judgment herein entered with said Clerk in this action on June 3, 1943, as adjudges that the plaintiff have and recover of the defendants, the State of New York and Saratoga Springs Commission, jointly, the sum of Five Thousand Four Hundred Fifty-Four Dollars and Seventy-Seven Cents ($5,454.77), with interest at 51 cents per day from December 31, 1942 on $3,124.54, the tax, to date of entry, and the further sum of $28.86, the costs and expenses of the plaintiff.

Dated August 3, 1943.

Nathaniel L. Goldstein, Attorney-General of the State of New York, Attorney for Defendant State of New York, 216 State Capitol Building, Albany, N. Y.

To The Clerk of the United States District Court for the Northern District of New York and to Irving J. Higbee, Esq., United States Attorney.

[fol. 46] IN UNITED STATES DISTRICT COURT

NOTICE OF APPEAL OF DEFENDANTS, COMMISSION AND AUTHORITY—July 20, 1943

[Title omitted]

Notice is hereby given that Saratoga Springs Commission, one of the defendants above named, hereby appeals to the Circuit Court of Appeals for the Second Circuit from so much of the judgment herein entered with the Clerk of the United States District Court for the Northern District of New York, at Utica, New York, in this action on May 12, 1943, and from so much of the amended judgment entered with said Clerk in this action on June 3, 1943, and from each and every part thereof, as adjudges that the plaintiff have and recover of the defendants the State of New York and Saratoga Springs Commission jointly the sum of Five Thousand Four Hundred Fifty-Four Dollars and Seventy-Seven Cents ($5,454.77), with interest at 51 cents per day from December 31, 1942, on $3,124.34, the tax to date of entry, and the further sum of $28.86, the costs and expenses of the plaintiff, and further

Notice is hereby given that Saratoga Springs Authority, one of the defendants above named, hereby appeals to [fol. 47] the Circuit Court of Appeals for the Second Circuit from so much of said judgment and said amended judgment herein, and from each and every part thereof, as adjudges that the plaintiff also have and recover of the defendant Saratoga Springs Authority the sum of Two Thousand Eight Dollars and Forty-Four Cents ($2,008.44), with interest on the tax of $1,203.47 at 29 cents per day from December 31, 1942, to date of entry.

Dated July 20, 1943.

Denis J. Harrington, Attorney for Defendants, Saratoga Springs Commission and Saratoga Springs Authority, Appellants, 398 Broadway, Saratoga Springs, N. Y.

To The Clerk of the United States District Court, Northern District of New York and to Irving J. Higbee, United States Attorney.

In United States District Court

Stipulation of Record—September 1, 1943

It is hereby stipulated that the foregoing printed record contains a full, true and correct record of the pleadings [fol. 48] and stipulation necessary for the determination of the appeal herein, including the opinion or decision of the United States District Judge filed herein, and that the Clerk of the U. S. District Court for the Northern District of New York shall make return thereof and file the same with the United States Circuit Court of Appeals for the Second Circuit without further comparison as and for a complete and true transcript of the record on the appeal in said cause.

Dated September 1, 1943.

Irving J. Higbee, United States Attorney, Attorney for Plaintiff-Appellee. Nathaniel L. Goldstein, Attorney General, Attorney for Defendant, State of New York, Appellant. Denis J. Harrington, Attorney for Defendants, Saratoga Springs Commission, and Saratoga Springs Authority, Appellants.

[fols. 49-58] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 50] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1943

No. 124

(Argued December 16, 1943 Decided February 7, 1944)

UNITED STATES OF AMERICA, Plaintiff-Appellee,

against

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY, Defendants-Appellants

Before:

L. Hand, Chase and Frank, Circuit Judges

Appeal by the defendants from a judgment of the District Court for the Northern District of New York in a suit brought by the United States to recover excise taxes. Affirmed.

[fol. 51] Samuel O. Clark, Jr., Assistant Attorney General; Sewall Key, J. Louis Monarch, Paul R. Russell, Special Assistants to the Attorney General; Irving Higbee, United States Attorney; B. F. Tompkins, Assistant United States Attorney for Plaintiff-Appellee.

Nathaniel L. Goldstein, Attorney General of The State of New York, Attorney for Defendant-Appellant; Orrin G. Judd, Solicitor General; Wendell P. Brown, First Assistant Attorney General; Henry S. Manley, Assistant Attorney General, Of Counsel.

Denis J. Harrington, Attorney for Saratoga Springs Commission and Saratoga Springs Authority; John A. Slade, of Counsel.

CHASE, *Circuit Judge:*

This appeal is from a judgment for the plaintiff entered in the District Court for the Northern District of New York in a suit by the United States to recover taxes, with interest thereon, levied against the three defendants under §615 (a) (5) of the Revenue Act of 1932, c. 209, 47 Stat. 169 on sales of bottled mineral and table waters taken from the springs at the State Reservation in Saratoga, N. Y. The defense was that the Saratoga Springs Authority is immune from such taxation as an agency of the state of New York engaged

in the performance of a governmental function of a nontaxable character.

The facts which were stipulated may be summarized as follows: From colonial times the waters found at Saratoga Springs have been recognized to possess marked medicinal value by virtue of the presence of various minerals, and they have been extensively used for drinking and bathing [fol. 52] purposes. The springs were exploited by private enterprise until 1912, but unwise operation was taking its toll by lowering the water level to an alarming extent and in that year the state stepped in to prevent that. To preserve and to restore them to their former flow, the state acquired title to all the land on which the springs were located, and took immediate measures to return the subterranean water level to a height from which it had been lowered by the drilling of new wells while the business was privately conducted.

In 1916 the State Department of Conservation was given custody of the lands, but in 1930 control was put in a newly-created Saratoga Springs Commission, a public commission of the State of New York and one of the defendants in this case. In 1933 the Saratoga Springs Authority, a public benefit corporation of the State of New York, took over the management and control of the premises by lease from the Commission. Large sums have been spent upon the improvement and maintenance of the springs, which are operated and made available to the people of New York and others, for the purpose of spreading widely the healthful benefits to be derived from the use of such waters.

To that end the Authority maintains on the premises a variety of establishments for the better utilization of the natural resources found in the springs. There are bath houses, tennis courts, drink halls, and a recreational center. Bus service is provided, and there is a hotel sanitarium operated by others under lease from the Authority.

The sale of bottled waters is promoted by extensive and costly advertising, and in recent years this enterprise has always yielded a substantial profit, with the exception of one year when a loss was sustained. The profits realized are applied to the expenses of maintaining the Reservation, which is not self-supporting and requires for its continued existence the aid of a large annual appropriation from the state legislature to pay the current deficits and to meet the

[fol. 53] interest and principal payments upon outstanding indebtedness.

The contention of the defendants is that the nature of this enterprise indicates that its operation is a governmental function of the State of New York immune from taxation.

The levy which is the subject of this litigation is a tax of two cents per gallon laid upon the sale of bottled waters sold at more than 12½ cents per gallon. The district court held that the sales were not made in performing a non-taxable governmental function, and entered judgment for the United States. 48 F. Supp. 15.

The Supreme Court held in *Collector* v. *Day*, 11 Wall. 113, that state governments were entitled to immunity by constitutional implication from taxation by the nation of the exercise of functions which were essential to their existence as they were constituted when the Constitution was adopted and on the premise that salaries are exempt when paid by a state to its officers who perform functions which are themselves immune from federal taxation invalidated a tax upon the salary of a state probate judge. But this case has recently been disapproved if not altogether overruled. *Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466. And it is clear that where a state engages in business in competition with private enterprise it enjoys no special privilege so far as immunity from federal taxation is concerned. *South Carolina* v. *United States*, 199 U. S. 437. But exactly where the line is to be drawn remains a problem by no means easy to solve and a variety of tests have been proposed from time to time.

In the *South Carolina* case, *supra*, the Supreme Court decided that immunity attached to activities of a strictly governmental character. In *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 172, the line was drawn at essential governmental functions. *Helvering* v. *Powers*, 293 U. S. 214, 225, spoke of usual governmental functions. The touchstone was held [fol. 54] to be traditional activities in *United States* v. *California*, 297 U. S. 175, 185. And in *Allen* v. *Regents*, 304 U. S. 439, 451, the court said it was a question whether the activity corresponded in all its essentials to a business usually carried on by private enterprise.

It will be noted that all those tests are more or less similar, yet they are not different ways of expressing quite the same idea. We think the fundamental consideration must be that exemption from federal taxation in a particular case flows

from the necessity to protect the continued existence of a state. *Cf. Helvering* v. *Gerhardt*, 304 U. S. 405, 421. The need of the state activity to maintain the states as they exist in our system of dual sovereignty will loom as the paramount issue, and whether any activity is described as essential or usual or traditional or something else will not weigh very heavily except as it bears upon that.

Turning now to the precise question here presented we are unable to distinguish as a permissible subject of federal taxation the business of a state engaged in bottling and selling water, a common private enterprise, from the business of a state engaged in selling some other potable like intoxicating liquor, also a common private enterprise. As the last mentioned activity is undoubtedly taxable by the federal government, *South Carolina* v. *United States, supra; Ohio* v. *Helvering*, 292 U. S. 360, so is the first. Much is made by defendants of the great value to public health, which is afforded by the springs, and we heartily agree that the enterprise is an extremely worthy one which benefits in great measure the people of New York as well as those from other states who visit the reservation. But it is not the maintenance of the health resort which is taxed. Nor does it seem possible to make a sound distinction between this case and those just cited on the ground that this water so bottled and sold is from a surplus resulting from the conservation and maintenance of a natural resource. It cannot [fol. 55] be denied that it is the limitation of the amount of water taken from the springs which preserves them for present and future use; not whether water withdrawn is bottled in part and sold. Equally immaterial to the same subject is whether the bottling and selling, if done, is done by a state agency or privately as formerly. Except for the profit the state derives from the business, all that it accomplishes in the conservation of a natural resource and in making the spring water available to the public could be done without making any charge for bottled water. When it engages in selling the bottled water the Saratoga Springs Authority is engaged in business for profit in competition with others in like business and subject to like federal taxation.

It is argued that *Mayo* v. *United States*, 319 U. S. 441, is contrary but we can perceive no conflict with the principles here given effect. In the *Mayo* case the issue was whether a Florida statute imposing an inspection fee designed to main-

tain the desired quality of fertilizer used on land in that state could be enforced in respect to shipments of fertilizer into Florida to be distributed under the supervision of the Secretary of Agriculture in carrying out the provisions of the Soil Conservation and Domestic Allotment Act, 49 Stat. 163, 1148; 50 Stat. 329; 55 Stat. 257, 860; 56 Stat. 664. It was held that, as in so doing the United States was carrying out a governmental function upon which the inspection fee was a direct burden, it was a tax which could not be laid by a state in the absence of consent by Congress, a quite different issue from that presented here. For any lawful function of the federal government in the performance of which the United States acts directly is constitutionally immune from state taxation, unless Congress consents, whereas only a limited class of state activities are constitutionally immune from federal taxation.

Judgment affirmed.

[fol. 56] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York on the 23rd day of February, one thousand nine hundred and forty-four.

Present: Hon. Learned Hand, Hon. Harrie B. Chase, Hon. Jerome N. Frank, Circuit Judges.

UNITED STATES OF AMERICA, Plaintiff-Appellee,

vs.

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY, Defendants-Appellants

Appeal from the District Court of the United States for the Northern District of New York.

This cause came on to be heard on the transcript of record from the District Court of the United States for the Northern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

Alexander M. Bell, Clerk.

[fol. 57] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. United States of America, v. State of New York and Saratoga Springs Commission and Saratoga Springs Authority. Order for Mandate. United States Circuit Court of Appeals: Second Circuit. Filed Feb. 23, 1944. Alexander M. Bell, Clerk.

[fol. 58] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 59] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1944

No. 83

[Title omitted]

ORDER ALLOWING CERTIORARI—Filed June 12, 1944

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on Cover: File No. 48,489, U. S. Circuit Court of Appeals, Second Circuit, Term No. 83. State of New York and Saratoga Springs Commission and Saratoga Springs Authority, Petitioners, *vs.* The United States of America. Petition for a writ of certiorari and exhibit thereto. Filed May 12, 1944. Term No. 83, O. T. 1944.

FILE COPY

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FILED
MAY 12 1944.
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

October Term, 1943.

No. [redacted] 5

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS, SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

NATHANIEL L. GOLDSTEIN,
Attorney General of the State of New York,
Attorney for Petitioners.

BATAVIA TIMES, LAW PRINTERS,
BATAVIA, N. Y.

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Supreme Court of the United States

October Term, 1943.

No. .....

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI.

To the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petitioners above named represented by Nathaniel L. Goldstein, Attorney General of the State of New York, respectfully pray that a writ of certiorari be issued from the Supreme Court of the United States directed to the Circuit Court of Appeals for the Second Circuit commanding that Court to certify for review and determination a transcript of the record and all proceedings in the case numbered and entitled on its docket, No. 124, October Term, 1943, United States of America, plaintiff-appellee, v. State of New York and Saratoga Springs Commission and Saratoga Springs Authority, defendants-appellants, and that the judgment of the Circuit Court of Appeals and the judg-

ment of the District Court may be reversed, and that the petitioners may have such other and further relief as may be just and proper.

Statement of the Case.

This suit was brought by the United States in its District Court for the Northern District of New York against the State and its agencies for collection of tax in excess of $3,000 imposed by the United States upon sales of bottled mineral water by the State and its agencies. The State has defended upon the ground that it is selling a natural resource which it owns, incidentally to a larger program related to the health and welfare of its citizens, which has long been a matter of State concern, and that such sales are constitutionally immune from taxation.

The complaint (R. 3-8) was met by answers (R. 9-15) and the facts were stipulated (R. 15-32).

The decision of the District Court was for the plaintiff (R. 32-39), and judgment was entered against the defendants (R. 41-44). Upon appeals by the defendants (R. 44-47) the Circuit Court of Appeals affirmed.

Opinions Below.

The opinion of the District Court (R. 32-39) is reported in 48 F. Supp. 15. The opinion of the Circuit Court of Appeals, dated February 7, 1944, is reported in 140 F. (2d) 608.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on February 23, 1944. The jurisdiction of the Supreme Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (U. S. C. A. Title 28 § 347).

Statutes Involved.

The federal act directly involved is the Revenue Act of 1932, section 615 (a) (5), which is as follows:

> "There is hereby imposed * * * (5) upon all natural or artificial mineral waters or table waters, whether carbonated or not, and all imitations thereof, sold by the producer, bottler or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of 2 cents per gallon." (47 Stat. 265.)

Paragraph 26 of the Stipulation of Facts (R. 31-32) lists several New York statutes relative to the Saratoga Springs reservation, of various years commencing with 1909. The following excerpts from Ch. 866 of N. Y. Laws of 1930 will serve as an illustration of their general purport:

> "A temporary state commission, to be known as the Saratoga Springs commission, is hereby created * * * for the purpose of ultimately developing the Saratoga Springs reservation as a state health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes. The development of such reservation for public health purposes is hereby declared a policy of the state * * *.
>
> "The commission shall have the power and it shall be its duty, subject to the provisions of this act, to conserve, maintain, control and develop each and every part of the reservation property. * * * The commission may prescribe the terms upon which any excess of mineral water and gas not used on said reservation or used under said leases or concessions, shall be sold or distributed, and shall prescribe the names, labels and advertisements to be affixed to the bottles or other vessels containing such waters, gases or other products, and may itself sell or dispose of the same. * * * The commission may make or cause to be made scientific studies and experiments concerning kinds of illnesses and diseases which lend themselves to the treatment of the mineral waters, products and facilities of the reservation, and shall exercise exclusive control and supervision over the manner and method or the use of the products and facilities of the reservation.

"The commission is hereby authorized and empowered to maintain and conduct the bath houses now on said reservation and such other bath houses as the commission may from time to time cause to be erected; to maintain and conduct the drink-hall or halls on said reservation and such others as may be built under the supervision of the commission; and also to maintain and conduct the bottling plant now on said reservation and is further authorized and empowered to enlarge or rebuild the same or construct a new and more adequate one as, in its discretion, will be most advantageous.

"The commission shall deposit at least once in each week in the depository or depositories designated by the [state] comptroller all moneys received by it for all purposes."

Summary Statement of Matter Involved.

The stipulation which occupies about seventeen pages of the record (R. 15-32) is the best source, and the following is merely a general outline, with a few of the facts most immediately relevant.

Commencing in 1911, when the ancient springs had become greatly impaired under private operation, the State undertook the purpose of preserving and restoring them and making them of greatest usefulness (R. 20). It has expended nearly $9,000,000 for lands and improvements, of which $3,200,000 was borrowed by the Authority from the RFC, and has appropriated various other sums for current expenses and interest payments. The total annual operating receipts of the Commission and Authority have never been sufficient to meet annual expenses, even after excluding interest and amortization charges on the RFC loan (R. 30).

Of the numerous related activities which make up that aggregate deficit, the one producing the greatest net in-

come is the lease of the Gideon Putnam Hotel Sanitarium, and the two largest items of gross income, excepting appropriations by the Legislature, are from admissions to the bath houses and sales of the bottled waters (R. 31).

The gross receipts from sales of bottled waters averaged about $125,000 annually from 1932 to 1941 (R. 23), from which certain expenses including advertising (R. 24) were deducted, but not depreciation or other capital expenses, resulting in a profit which averaged slightly over $16,000 annually in those years (R. 27-28).

The consistent policy of the Commission and the Authority has been to increase the volume of waters bottled and sold and derive the largest profit possible from this activity, in order that the proceeds might be applied to the cost of other services rendered at the Spa (R. 26-27). The "profit" averaging over $16,000 annually, mentioned above, was thus applied (R. 28).

Three mineral waters and one plain water are bottled and sold, and were during the period covered by the assessments, all in their natural state. The mineral waters are Hathorn, a laxative water; Coesa, a diuretic water; and Geyser, a digestive water. These are properly classified as mineral waters; they are not suitable for indiscriminate beverage use and cannot be mixed with fruit juices or alcoholic beverages. The plain water, known as State Seal, is a high chemical and vegetable purity. It is used very largely in various state institutions and offices, and a small amount is also purchased by the general public, mostly on recommendation of physicians (R. 22). About 50% of the total waters upon which the tax was levied were handled by one distributor in New York City and vicinity, but smaller amounts were sold elsewhere in New York State and in other states (R. 23-34).

Question Presented.

Does the taxing power of the United States extend to moneys in the hands of a State received by it from sales of a natural resource which it owns, such sales being made incidentally to a larger program related to the health and welfare of its citizens which has long been a matter of concern to the State?

Reasons Relied on for Allowance of the Writ.

A.

The Courts below have decided the foregoing question in the affirmative. Their opinions indicate that they are presently without any guide as to how much, if any, of the state immunity from federal taxation declared in *Collector* v. *Day*, 11 Wall. 113 (1870), and cases following it, remains since the personal income tax aspect of that decision was disapproved in *Graves* v. *N. Y. ex rel. O'Keefe*, 306 U. S. 466 (1939).

B.

It is the contention of the petitioners that the Circuit Court of Appeals has decided an important question of federal law which has not been, but should be, decided by the Supreme Court. The Circuit Court of Appeals in the final paragraph of its opinion asserted the present rule to be that "any lawful function" of the United States is constitutionally immune from state taxation, but "*only a limited class of state activities*" (those necessary "*to protect the continued existence of a state*," according to an earlier paragraph) are similarly immune from federal taxation. It is submitted that this test for state immunity is valueless, inasmuch as there is no minimum standard of what constitutes the "continued existence of a state";

moreover, this test is not authorized by the decisions of the Supreme Court.

C.

It is further contended that the Circuit Court of Appeals has decided a federal question in a way probably in conflict with decisions of the Supreme Court, insofar as there is involved the validity of a federal tax imposed upon sale by a state of natural resources owned by it. The case of *Helvering* v. *Producers Corp.*, 303 U. S. 376 (1938), and the earlier cases of taxation of proceeds from oil leases cited therein, all assume that such proceeds when derived by a state and in its hands are immune from federal taxation.

BRIEF SUPPORTING PETITION.

The following argument is offered in expansion of the three grounds previously stated.

The source of all discussion upon the reciprocal tax immunities inferred from the dual sovereignties of the federal Constitution is the opinion of Chief Justice Marshall in *McCulloch* v. *Maryland*, 4 Wheat. 316 (1819), holding that a bank chartered by the United States was immune from a Maryland stamp tax imposed on the bank's circulating currency, and Mr. Justice Nelson's opinion in *Collector* v. *Day*, 11 Wall. 113 (1870), holding the salary of a Massachusetts judge immune from a federal income tax. In the latter case the basis of the inferred immunities was stated as follows:

> "It is admitted that there is no express provision in the Constitution that prohibits the general government from taxing the means and instrumentalities of the States, nor is there any prohibiting the States from taxing the means and instrumentalities of that govern-

ment. In both cases the exemption rests upon necessary implication, and is upheld by the great law of self-preservation; as any government, whose means employed in conducting its operations, if subject to the control of another and distinct government, can exist only at the mercy of that government. Of what avail are these means if another power may tax them at discretion?" (11 Wall. p. 127.)

Within the past ten years there has been great increase of authorities, stemming from those cases and that doctrine. The reasons for this phenomenon are prudently left for historians to determine and declare—it is a sufficient evil for the present day to note the numbers of authorities and their inconsistencies of formula and result.

The courts in eight cases prior to 1939 invalidated the following taxes:

(1) A federal stamp tax on bonds required by state law from licensed liquor dealers. *Ambrosini* v. *United States*, 187 U. S. 1 (1902).

(2) A federal tax upon the income of an employee of a municipally-operated street railway. *Frey* v. *Woodworth*, 2 F. 2d 725 (D. C. Mich., 1924), error dis. 270 U. S. 669 (1926).

(3) A federal sales tax on a motorcycle sold to a municipality for its police department. *Indian Motocycle Co.* v. *United States*, 283 U. S. 570 (1930).

(4) A federal tax upon income of a lessee derived from oil produced from school lands held in trust by the state and leased by it. *Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393 (1931).

(5) A federal tax upon the salary of a superintendent of public parks. *Commissioner* v. *Sherman*, 69 F. 2d 755 (C. C. A., 1st, 1934).

(6) A federal tax upon the salary of a superintendent of a public school cafeteria. *Hoskins* v. *Commissioner*, 84 F. 2d 627 (C. C. A., 5th, 1936).

(7) A federal tax upon the income of an employee of a municipal water supply bureau. *Brush* v. *Commissioner*, 300 U. S. 352 (1937).

(8) A federal tax upon the salary of a member of a state commission engaged in constructing and operating a bridge. *Bower* v. *Glenn*, 21 F. Supp. 766 (D. C., Ky., 1938), ap. dis. 107 F. 2d 1013 (1938).

Meanwhile, in eleven other cases, the courts have sustained the following taxes:

(1) A federal license tax upon state-owned liquor dispensaries. *South Carolina* v. *United States*, 199 U. S. 437 (1905).

(2) A federal excise tax upon private corporations organized under state laws. *Flint* v. *Stone Tracy Co.*, 220 U. S. 107 (1910).

(3) A federal tax upon compensation paid by a state to engineers engaged in supervising construction of a municipal water supply and sewage disposal system. *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514 (1925).

(4) A federal income tax on capital gains derived from sales of municipal bonds. *Willcuts* v. *Bunn*, 282 U. S. 216 (1930).

(5) A federal tax upon the lessee's income derived from resale of oil produced by state lands, under a lease which effected a present sale of the oil in the ground to the lessee. *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279 (1930).

(6) A federal tax upon the lessee's income from oil lands leased by a municipality. *Burnet* v. *Jergin Trust Co.*, 288 U. S. 508 (1932).

(7) A federal license tax upon state-owned liquor stores. *Ohio* v. *Helvering*, 292 U. S. 360 (1934).

(8) A federal tax upon compensation of a member of the Board of Trustees of Boston Elevated Railway. *Helvering* v. *Powers*, 293 U. S. 214 (1934).

(9) A federal tax upon the lessee's income derived from oil produced by state school lands. *Helvering* v. *Mountain Producers Corp.*, 303 U. S. 376 (1938).

(10) A federal tax upon the salary of an employee of the Port of New York Authority. *Helvering* v. *Gerhardt*, 304 U. S. 405 (1938).

(11) A federal tax upon admissions to athletic contests conducted by a state university. *Allen* v. *Regents*, 304 U. S. 439 (1938).

This list is probably incomplete, but at least is representative.

During the 1930's the crop of adjudication arising from the immunity doctrine became so luxuriantly uncontrolled that nearly all of it was disapproved in 1938-1939.

Since the decision of *Graves* v. *N. Y. ex rel. O'Keefe*, 306 U. S. 466 (1939), which expressly overruled the doctrine of constitutional immunity from *indirect* burdens, most notably the burden previously assumed to exist by reason of a tax upon a salary of a governmental employee or officer, or upon one contracting with government to supply it with goods or perform services for it, the nineteen cases listed, which already were fighting amongst themselves, have with three exceptions been overwhelmed. None of the eight cases first listed, wherein the decision was against the federal tax, involved such a tax imposed directly upon the property or activity of a state. All were upon persons acting under state law, or employees of a state, or persons

doing business with it. So also with all cases in the second list, except *South Carolina* v. *United States*, and *Ohio* v. *Helvering* (the federal license taxes imposed upon state-operated liquor stores), and *Allen* v. *Regents*, (the federal tax upon admissions to athletic contests conducted by a state university).

This is not supposed to mean that there remains no doctrine of immunity of state property and activities from federal taxation. On the contrary, the majority opinion by Mr. Justice Stone in the *O'Keefe* case continued to talk of "the constitutional immunity of *either* government from taxation by the other" (306 U. S. p. 480, emphasis added), and said of the *Gerhardt* case that it was properly held that the salaries of the employees of the Authority were not immune, "even though the Authority be regarded as not subject to federal taxation" (p. 484). There was discussion of possible differences between state immunity and federal immunity (p. 485); the basis for overruling *Collector* v. *Day* and similar decisions was said to be the unwarranted assumption that the tax burden placed upon another actually burdened the government by which he was employed or with which he dealt (pp. 483, 486), and that case was overruled only to the extent made appropriate by that consideration (pp. 486-487). In the concurring opinion of Mr. Justice Frankfurter, also, it was only the "sterile refinements" (p. 488) and the "interdependent doctrine" (p. 492) which were condemned; the reason and force of the underlying doctrine was stated as follows:

> "Since two governments have authority within the same territory, neither through its power to tax can be allowed to cripple the operations of the other. Therefore state and federal governments must avoid exactions which discriminate against each other or obviously interfere with one another's operations." (p. 488.)

Likewise in *Mayo* v. *United States*, 319 U. S. 441, 447 (1943) Mr. Justice Reed said of the freedom of a federal activity from state taxation:

> "This freedom is inherent in sovereignty."

And in *United States* v. *County of Alleghany*, on May 1, 1944, Mr. Justice Jackson said:

> "The trend of recent decisions has been to withdraw private property and profits from the shelter of governmental immunity but without impairing the immunity of the State or the Nation itself."

There remains, then, a doctrine of immunity of state property and activities from federal taxation, its essential vigor unimpaired, but its application very uncertainly defined.

In the more recent decisions on tax immunity the favored test has been that of "*direct burden.*" Thus, in *Mayo* v. *United States* it was said that the objectionable inspection fees "are laid *directly* upon the United States." (319 U. S. at p. 447, italics added). In the *County of Alleghany* case all three opinions acknowledged the test, although Mr. Justice Roberts was of opinion that it was not being followed. The brief for the United States in *Alabama* v. *King & Boozer*, 314 U. S. 1 (1941) disclaimed all tests for immunity except whether the tax was nondiscriminatory and whether it was imposed upon the government or a private person. The opinion by the Chief Justice approved the test selected, and disagreed with the attorneys for the United States as to the incidence of the tax. The *O'Keefe* and *Gerhardt* cases certainly hold that income tax imposed upon salaries of employees is not a "direct burden" upon the employing government. The following statement from the *O'Keefe* opinion speaks for both:

> "The burden on government of a non-discriminatory income tax applied to the salary of the employee of a

government or its instrumentality is the same, whether a state or national government is concerned." (3066 U. S. at p. 485.)

Oddly enough, in the present case the United States did not rely upon the "direct burden" test, but upon the "governmental function" test, for which it cited the *Gerhardt* case. See the comment of the District Court that the plaintiff, "finds particular comfort, if not the whole support for its position," in that case and three earlier ones (R. 37). The same cases are considered in the opinion of the Circuit Court of Appeals, leading to this statement:

> "We think the fundamental consideration must be that exemption from federal taxation in a particular case flows from the necessity to protect the continued existence of a state. Cf. *Helvering* v. *Gerhardt*, 304 U. S. 405, 421. The need of the state activity to maintain the states as they exist in our system of dual sovereignty will loom as the paramount issue, and whether any activity is described as essential or usual or traditional or something else will not weigh very heavily except as it bears upon that."

A warning against all such tests is found in the majority opinion in *Brush* v. *Commissioner*, 300 U. S. 352, 361-364 (1937), and the double test of non-discrimination and direct burden is outlined in the dissent of Mr. Justice Roberts (p. 375). Mr. Justice Black has also criticized the test of "essential government functions" in his concurring opinion in the *Gerhardt* case, 304 U. S. at pp. 426-427. The doctrine that all activities of the federal government, including the bank involved in *McCulloch* v. *Maryland* and many more recent and novel businesses, are necessarily governmental, but identical activities of a state are proprietary, lacks a sense of reality. As Mr. Justice Black said, it is the people acting through Congress and the state legislatures who determine, as conditions demand, what services and functions the public welfare demands (304 U. S. p. 427).

Although the majority opinion in the *Gerhardt* case contained a lengthy discussion of the "nature" of the state activity involved—the Port of New York—it does not really support that test. Illustrative of its indefinite basis, is this caveat contained in the opinion:

> "Expressing no opinion whether a federal tax may be imposed upon the Port Authority itself with respect to its receipt of income or other activities, we decide only that the present tax neither precludes nor threatens unreasonably to obstruct any functions essential to the continued existence of the State government." (p. 424.)

But when the *O'Keefe* case was decided ten months later, and the *Gerhardt* case was discussed in its opinion, there was no longer talk of the "nature" of the activities involved, but only of the incidence of the tax. See 306 U. S. p. 484.

The reason why the United States did not rely upon the "direct burden" test in the present case, although it asserted its superiority in the recent cases of *Mayo* and *King & Boozer*, is to be found in the nature of the present case.

If, as here, a tax is levied directly upon money in the hands of the State derived from its sale of its natural resources, little question remains about the incidence of the tax.

Petitioners submit that it is the essence of sovereignty for a state to be able to dispose of its property. Possessed of much property, whether originally owned or acquired with time, the states as a traditional, usual and necessary practice have owned and disposed of this property. Land, water, oil, coal, gold, gravel in river beds, are but a few of the natural resources that the states have sold. Public welfare is subserved by making the resources of the state available for enjoyment by the people, and the proceeds

from the sale of such property are revenue to carry on other governmental functions. If the states and federal government were to tax each other because of the ownership and sale of their respective natural resources, the burden upon government itself would be apparent.

Hence, it is not surprising that the Courts have without question considered this governmental activity as one removed from the taxing power of the other sovereign. Thus, in *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279 (1930), where the Court sustained a federal tax upon profits derived by a lessee from the sale of oil and gas produced on lands leased by the State of Texas, the Court said (p. 282):

> "Property sold or otherwise disposed of by the government, either state or national, in order to raise revenue for government purposes, is in a broad sense a government instrumentality, with respect to which neither the property itself before sale, nor its sale by one government, may be taxed by the other."

More recently the Court reexamined the question of taxing the gains of lessees of state or federal lands in *Helvering* v. *Mountain Producers' Corporation*, 303 U. S. 376 (1938). The Court recognized the distinction between a tax upon the state and a tax upon the lessee when it framed the issue before it thus (p. 384):

> "whether, in a case where a tax is not laid upon the the *leases* as such, or upon the *government's property* or interest, but is imposed upon the gains of the lessee, like that laid upon others engaged in similar business enterprises, there is in truth such a direct and substantial interference with the performance of the government's obligation as to require immunity for the lessee's income." (Emphasis supplied.)

Petitioners do not suppose that it is contended that the federal government may tax the income the states realize from leases of lands containing saleable natural resources. Is the state to be burdened because as a matter of state

policy it is thought more desirable to dispose of these resources as a continuous state activity? Or conversely, if the federal government chose to produce and sell the oil on Indian lands, could the State tax the sale thereof or income produced thereby?

The case at bar presents such a situation. Involved here is a federal tax upon the sale by the State of its natural resources. The incidence of the tax is directly upon the State. Without reviewing all of the facts contained in the statement, petitioners point out that the sale of these natural waters by the petitioners is not an isolated activity, but merely a small part of a larger program of conservation of natural resources, promotion of health and creation of recreation facilities.

The distinction, therefore, between the case at bar and the cases cited by the District Court and the Circuit Court of Appeals is readily apparent. In *South Carolina* v. *United States*, 199 U. S. 437; *Ohio* v. *Helvering*, 292 U. S. 360; *Helvering* v. *Powers*, 293 U. S. 214, and *Allen* v. *Regents*, 304 U. S. 439, the respective state was not engaged in the disposition of its natural resources. In the *South Carolina* and *Ohio* cases, the states bought and sold liquor; in the *Powers* case the state merely took over the management of an existing railway; in the *Regents* case the state constructed two stadia seating about 30,000 people each for universities whose student bodies were about 2,000 each, and sold admissions (304 U. S. p. 450). Anybody seeking an analogy to those facts will find one, not in the disposition of the spring waters at Saratoga, but in the summer theatre, the swimming pool, the golf course, or the hotel constructed on the Reservation, if all these activities were operated by the Commission.

It was urged by the United States herein that the absence of profits or the fact that profits from the sale of waters

are used to defray the expenses of the Reservation will not immunize the sales. Petitioners similarly contend that the fact that profits *are* realized from the sales does *not* deprive them of their immunity. As the Court said in *Brush* v. *Commissioner,* 300 U. S. 352, 372-373 (1936):

> "If that service be governmental it does not become private because a charge is made for it, or a profit realized. A state, for example, constructs and operates a highway. It may, if it choose, exact compensation for its use from those who travel over it (see *Bingham* v. *Golden Eagle Lines,* 297 U. S. 626, 628); but this does not destroy the claim that the maintenance of the highway is a public and governmental function. The state or the city may exact a tuition charge for instruction in the public schools; but thereby the maintenance of the public schools does not cease to be a function of the government. The state exacts a fee for issuing a license or granting a permit; for recording a deed; for rendering a variety of services in the judicial department. Do these various services thereby lose their character as governmental functions? The federal Post Office Department charges for its services; but no one would question the fact that its operation calls into exercise a governmental function."

Petitioners here point out that in the *South Carolina* case, the source of all adverse authorities, one of the most powerful considerations was the Court's fear that if the liquor business were free from federal taxation, the State might enter other businesses and thus destroy a large source of federal revenue. That consideration is certainly not present in the case at bar. If this Court should hold that the State may sell its natural mineral waters free from federal tax, there is no need to fear that the State may exercise its police powers in other fields of activity and thus limit the sources of federal revenue. The number of natural resources is not large and, thus, the list of immune activities rather limited. Furthermore, with respect to the particular facts of the case at bar, it is to be noticed that

the State did not acquire the springs at Saratoga to bottle and sell the waters. In fact, although the first legislation creating the board known as "The Commissioners of the State Reservation at Saratoga Springs" gave it the power to sell the excess of mineral water not used on the premises (L. 1909, ch. 569, Sec. 5), it was not until 1930 that the successors of this original board exercised that power.

Again, it is to be noticed that on the facts of the case at bar the sale of these natural waters is not an isolated activity, but is related to a particular program of conservation, health, and recreation. Petitioners recognize that the Court, in *Allen* v. *Regents*, was not persuaded to exempt football tickets from a federal tax because the proceeds of the exhibition were used to finance the State educational program. But the tax in that case was not against the State which was merely the collecting agency for the tax which was payable by the purchaser of the ticket and not as here by the State itself. Mention is made of the larger program at Saratoga Springs, however, because it is only in connection with that program that the State decided to sell these waters. Thus, to grant immunity in the case at bar does not necessarily require immunity when the State engages in a wholesale disposition of its natural resources, unrelated to any particular public program.

Petitioners see no reason why the taxing power of the federal government will be seriously impaired if the sale of Saratoga mineral waters is free from tax. On the other hand, to hold this activity within the scope of the federal taxing power might seriously hamper the operation of the program of conservation, health and recreation at the Spa.

Conclusion.

For the three reasons stated at pages 6-7 of this petition and brief, supported by the discussion of relevant decisions

contained herein, it is respectfully submitted that the petition for a writ of certiorari in the instant case should be granted.

Albany, May 4, 1944.

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Supreme Court of the United States

OCTOBER TERM, 1944

No. [redacted] 5

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

THE UNITED STATES OF AMERICA.

BRIEF FOR THE STATE OF NEW YORK, PETITIONER

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Supreme Court of the United States

OCTOBER TERM, 1944

No. 83

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

THE UNITED STATES OF AMERICA.

BRIEF FOR THE STATE OF NEW YORK, PETITIONER

Jurisdiction

Certiorari was granted by this Court on June 12, 1944, to review the judgments of the Circuit Court of Appeals for the Second Circuit and of the District Court herein.

Opinions Below

The opinion of the District Court (R. 22-26) is reported in 48 F. Supp. 15. The opinion of the Circuit Court of Appeals (R. 33-37) is reported in 140 F. (2d) 608.

Statement of the Case

This suit was brought by the United States in its District Court for the Northern District of New York against the State and its agencies for collection of tax in excess of $3,000 imposed by the United States upon sales of bottled mineral water by the State and its agencies. The State has defended upon the ground that it is selling a natural resource which it owns, incidentally to a larger program related to the health and welfare of its citizens, which has long been a matter of State concern, and that such sales are constitutionally immune from taxation.

The complaint (R. 2-6) was met by answers (R. 6-9) and the facts were stipulated (R. 9-21).

The decision of the District Court was for the United States upon the ground that the selling of Saratoga Springs mineral water was a 'business enterprise conducted for gain' (R. 22-26) and judgment was entered against the defendants, now petitioners (R. 27-30). Upon appeals (R. 30-31) the Circuit Court of Appeals affirmed, upon the ground that the claimed immunity was not justified by the test of 'necessity to protect the continued existence of a state' (R. 33-37).

The stipulation which occupies about twelve pages of the record (R. 9-21) is the best source for the facts, and the following is merely a general outline, with a few of the facts most immediately relevant.

Commencing in 1911, when the ancient springs at Saratoga had become greatly impaired under private operation, the State undertook the project of preserving and restoring them and making them of greatest public usefulness (R. 13). It has expended nearly $9,000,000 for lands and

improvements, of which $3,200,000 was borrowed by the Authority from the RFC, and has appropriated various other sums for current expenses and interest payments. The total annual operating receipts of the Commission and Authority have never been sufficient to meet annual expenses, even after excluding interest and amortization charges on the RFC loan (R. 20).

Of the numerous related activities which make up that aggregate deficit, the one producing the greatest net income is the lease of the Gideon Putnam Hotel-Sanitarium, and the two largest items of gross income, excepting appropriations by the Legislature, are from admissions to the bath houses and sales of the bottled waters (R. 21).

The gross receipts from sales of bottled waters averaged about $125,000 annually from 1932 to 1941 (R. 15), from which certain expenses including advertising (R. 16) were deducted, but not depreciation or other capital expenses, resulting in a profit which averaged slightly over $16,000 annually in those years (R. 18).

The consistent policy of the Commission and the Authority has been to increase the volume of waters bottled and sold and derive the largest profit possible from this activity, in order that the proceeds might be applied to the cost of other services rendered at the Spa (R. 17-18). The "profit" averaging over $16,000 annually, mentioned above, was thus applied (R. 19).

Three mineral waters and one plain water are bottled and sold, and were during the period covered by the assessments, all in their natural state. The mineral waters are Hathorn, a laxative water; Coesa, a diuretic water; and Geyser, a digestive water. These are properly classified as mineral waters; they are not suitable for indiscriminate

beverage use and cannot be mixed with fruit juices or alcoholic beverages. The plain water, known as State Seal, is of a high chemical and vegetable purity. It is used very largely in various state institutions and offices, and a small amount is also purchased by the general public, mostly on recommendation of physicians (R. 14). The waters of these springs have a recognized medical value, and are prescribed by physicians both for bathing and internal use (R. 12). About 50% of the total waters upon which the tax was levied were handled by one distributor in New York City and vicinity, but smaller amounts were sold elsewhere in New York State and in other states (R. 15).

Statutes Involved

The federal act directly involved is the Revenue Act of 1932, section 615 (a) (5), which is as follows:

> "There is hereby imposed * * * (5) upon all natural or artificial mineral waters or table waters, whether carbonated or not, and all imitations thereof, sold by the producer, bottler or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of 2 cents per gallon." (47 Stat. 265).

Paragraph 26 of the Stipulation of Facts (R. 21) lists several New York statutes relative to the Saratoga Springs reservation, of various years commencing with 1909. The following excerpts from Ch. 866 of N. Y. Laws of 1930 will serve as an illustration of their general purport:

> "A temporary state commission, to be known as the Saratoga Springs commission, is hereby created * * * for the purpose of ultimately developing the Saratoga Springs reservation as a state health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes. The development of such reservation for public health purposes is hereby declared a policy of the state * * *.

"The commission shall have the power and it shall be its duty, subject to the provisions of this act, to conserve, maintain, control and develop each and every part of the reservation property. * * * The commission may prescribe the terms upon which any excess of mineral water and gas not used on said reservation, or used under said leases or concessions, shall be sold or distributed, and shall prescribe the names, labels and advertisements to be affixed to the bottles or other vessels containing such waters, gases or other products, and may itself sell or dispose of the same. * * * The commission may make or cause to be made scientific studies and experiments concerning kinds of illnesses and diseases which lend themselves to the treatment of the mineral waters, products and facilities of the reservation, and shall exercise exclusive control and supervision over the manner and method of the use of the products and facilities of the reservation.

"The commission is hereby authorized and empowered to maintain and conduct the bath houses now on said reservation and such other bath houses as the commission may from time to time cause to be erected; to maintain and conduct the drink-hall or halls on said reservation and such others as may be built under the supervision of the commission; and also to maintain and conduct the bottling plant now on said reservation and is further authorized and empowered to enlarge or rebuild the same or construct a new and more adequate one as, in its discretion, will be most advantageous.

"The commission shall deposit at least once in each week in the depository or depositories designated by the [state] comptroller all moneys received by it for all purposes."

Specification of Error

The error asserted by the State against the decisions below is, of course, the fundamental error of having denied the tax immunity involved.

POINT I

The tax imposed is a direct burden upon a governmental function, and hence is constitutionally objectionable.

The principle of governmental immunity from taxation is sufficiently accepted as a principle, and sufficiently indefinite in its specific applications, so that the litigated cases tend to arise around the borders of the protected ground rather than squarely within its confines. As Mr. Justice Jackson observed in *United States* v. *Allegheny County*, 322 U. S. 174, 188: "Rarely does a state or municipality pursue the Federal Government itself." So it is in the present case that the facts do not present the problem with the utmost possible dramatic force; no claim will be made on behalf of the State that its existence will be terminated by the tax imposed. This concession is made at the beginning of argument, because the Circuit Court of Appeals seems to have regarded it as decisive, saying:

> "We think the fundamental consideration must be that exemption from federal taxation in a particular case flows from the necessity to protect the continued existence of a state." (R. 35-36).
>
> "For any lawful function of the federal government in the performance of which the United States acts directly is constitutionally immune from state taxation, unless Congress consents, whereas only a limited class of state activities are constitutionally immune from federal taxation." (R. 37).

Although not of itself a great threat to the existence of the State, it is submitted that the facts of the present case in no way fall short of a tax burden directly imposed upon the performance of a governmental function. Believing that the facts involve the principle of governmental immunity

and that the principle must be defended at its borders, the State has pressed the litigation to this Court.

A few citations will serve to trace the history of the principle sufficiently for present purposes.

The source of all discussion upon the reciprocal tax immunities inferred from the dual sovereignties of the Federal Constitution is the opinion of Chief Justice Marshall in *McCulloch* v. *Maryland*, 4 Wheat. 316 (1819), holding that a bank chartered by the United States was immune from a Maryland stamp tax imposed on the bank's circulating currency, and Mr. Justice Nelson's opinion in *Collector* v. *Day*, 11 Wall. 113 (1870), holding the salary of a Massachusetts judge immune from a federal income tax. In the latter case the basis of the inferred immunities was stated as follows:

> "It is admitted that there is no express provision in the Constitution that prohibits the general government from taxing the means and instrumentalities of the States, nor is there any prohibiting the States from taxing the means and instrumentalities of that government. In both cases the exemption rests upon necessary implication, and is upheld by the great law of self-preservation; as any government, whose means employed in conducting its operation, if subject to the control of another and distinct government, can exist only at the mercy of that government. Of what avail are these means if another power may tax them at discretion?" (11 Wall. p. 127)

The decision of *Graves* v. *N. Y. ex rel. O'Keefe*, 306 U. S. 466 (1939), expressly overruled *Collector* v. *Day*, but not the doctrine of immunity of state property and activities from federal taxation. On the contrary, the majority opinion by Mr. Justice Stone in the O'Keefe case continued to speak of "the constitutional immunity of *either* government from taxation by the other" (306 U. S. p. 480, emphasis added), and said of *Helvering* v. *Gerhardt*,

304 U. S. 405 (1938), that it was properly held that the salaries of the employees of the Port of New York Authority were not immune, "even though the Authority be regarded as not subject to federal taxation" (p. 484). There was discussion of possible differences between state immunity and federal immunity (p. 485); the basis for overruling *Collector* v. *Day*, and similar decisions was said to be the unwarranted assumption that the tax burden placed upon another actually burdened the government by which he was employed or with which he dealt (pp. 483-486), and that case was overruled only to the extent made appropriate by that consideration (pp. 486-487). In the concurring opinion of Mr. Justice Frankfurter, also, it was only the "sterile refinements" (p. 488) and the "interdependent doctrine" (p. 492) which were condemned; the reason and force of the underlying doctrine was stated as follows:

> "Since two governments have authority within the same territory, neither through its power to tax can be allowed to cripple the operations of the other. Therefore state and federal governments must avoid exactions which discriminate against each other or obviously interfere with one another's operations." (p. 488.)

Likewise in *Mayo* v. *United States*, 319 U. S. 441, 447 (1943) Mr. Justice Reed said of the freedom of a federal activity from state taxation:

> "This freedom is inherent in sovereignty."

And in *United States* v. *Allegheny County*, 322 U. S. 174, 186 (1944), Mr. Justice Jackson said:

> "The trend of recent decisions has been to withdraw private property and profits from the shelter of governmental immunity but without impairing the immunity of the State or the Nation itself."

There remains, then, a doctrine of immunity of state property and activities from federal taxation, its essential vigor unimpaired, but its application very uncertainly defined.

For purposes of determining whether the present case is within the application of the principle, a significant decision is *Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393 (1931), invalidating a federal tax upon income of a lessee derived from oil produced from school lands, held in trust by the state and leased by it. The facts that a different result was reached in *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279 (1930) and that the *Coronado* case was distinguished in *Burnet v. Jergins Trust*, 288 U. S. 508, 516 (1932) and overruled in *Helvering* v. *Producers Corp.*, 303 U. S. 376, 383 (1938) do not affect the significance of those decisions as showing that the sale by a state of its natural resources (in those cases petroleum), even though continuously over a period of time, is a governmental function which would have been immune from any taxation had it been directly imposed upon the proceeds in the hands of the state. All those decisions turned, as did the *Gerhardt* and *O'Keefe* decisions, upon the fact that the taxation in question was not a direct burden upon the state activity involved, and still support the position of the present brief that the sale continuously by a state of its natural resources is a governmental activity entitled to immunity.

In the more recent decisions on tax immunity the favored test has been that of "*direct burden.*" Thus, in *Mayo* v. *United States*, it was said that the objectionable inspection fees "are laid *directly* upon the United States." (319 U. S. at p. 447, emphasis added.) In the *County of Allegheny* case all three opinions acknowledged the test, although Mr. Justice Roberts was of opinion that it was not being fol-

lowed. The brief for the United States in *Alabama* v. *King & Boozer*, 314 U. S. 1 (1941), disclaimed all tests for immunity except whether the tax was non-discriminatory and whether it was imposed upon the government or a private person. The opinion by the Chief Justice approved the test selected, and disagreed with the attorneys for the United States as to the incidence of the tax. The *O'Keefe* and *Gerhardt* cases certainly hold that income tax imposed upon salaries of employees is not a "direct burden" upon the employing government. The following statement from the *O'Keefe* opinion speaks for both:

> "The burden on government of a non-discriminatory income tax applied to the salary of the employee of a government or its instrumentality is the same, whether a state or national government is concerned." (306 U. S. at p. 485.)

In the present case it seems clear that the "direct burden" test is satisfied, and the United States does not argue the contrary. Instead, it passes that question by and relies upon the "governmental function" test, for which it cited in the courts below the *Gerhardt* case. See the comment of the District Court that the plaintiff, "finds particular comfort, if not the whole support for its position," in that case and three earlier ones (R. 25). The same cases are considered in the opinion of the Circuit Court of Appeals, leading to this statement:

> "We think the fundamental consideration must be that exemption from federal taxation in a particular case flows from the necessity to protect the continued existence of a state. Cf. *Helvering* v. *Gerhardt*, 304 U. S. 405, 421. The need of the state activity to maintain the states as they exist in our system of dual sovereignty will loom as the paramount issue, and whether any activity is described as essential or usual or traditional or something else will not weigh very heavily except as it bears upon that." (R. 35-36.)

A warning against all such tests is found in the majority opinion in *Brush* v. *Commissioner*, 300 U. S. 352, 361-364 (1937), and the double test of non-discrimination and direct burden is outlined in the dissent of Mr. Justice Roberts (p. 375). Mr. Justice Black has also criticized the test of "essential government functions" in his concurring opinion in the *Gerhardt* case, 304 U. S. at pp. 426-427. The doctrine that all activities of the federal government, including the bank involved in *McCulloch* v. *Maryland* and many more recent and novel businesses, are necessarily governmental, but identical activities of a state are proprietary, lacks a sense of reality. As Mr. Justice Black said, it is the people acting through Congress and the state legislatures who determine, as conditions demand, what services and functions the public welfare demands (304 U. S. p. 427).

Although the majority opinion in the *Gerhardt* case contained a lengthy discussion of the "nature" of the state activity involved—the Port of New York—it does not really support that test. Illustrative of its indefinite basis, is this *caveat* contained in the opinion:

> "Expressing no opinion whether a federal tax may be imposed upon the Port Authority itself with respect to its receipt of income or its other activities, we decide only that the present tax neither precludes nor threatens unreasonably to obstruct any function essential to the continued existence of the state government." (p. 424).

But when the *O'Keefe* case was decided ten months later, and the *Gerhardt* case was discussed in its opinion, there was no longer mention of the "nature" of the activities involved, but only of the incidence of the tax. See 306 U. S. p. 484.

The reason why the United States did not rely upon the "direct burden" test in the present case, although it as-

serted its superiority in the recent cases of *Mayo* and *King & Boozer*, is to be found in the nature of the present case.

If, as here, a tax is levied directly upon money in the hands of the State derived from its sale of its natural resources, little question remains about the incidence of the tax.

The State submits that it is the essence of sovereignty for a state to be able to dispose of its property. Possessed of such property, whether originally owned or acquired with time, the states as a traditional, usual and necessary practice have owned and disposed of this property. Land, water, oil, coal, gold, gravel in river beds, are but a few of the natural resources that the states have sold. Public welfare is subserved by making the resources of the state available for enjoyment by the people, and the proceeds from the sale of such property are revenue to carry on other governmental functions. If the states and federal government were to tax each other because of the ownership and sale of their respective natural resources, the burden upon government itself would be apparent.

Hence, it is not surprising that the courts have without question considered this governmental activity as one removed from the taxing power of the other sovereign. Thus, in *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279 (1930), where the Court sustained a federal tax upon profits derived by a lessee from the sale of oil and gas produced on lands leased by the State of Texas, the Court said (p. 282):

> "Property sold or otherwise disposed of by the government, either state or national, in order to raise revenue for government purposes, is in a broad sense a government instrumentality, with respect to which neither the property itself before sale, nor its sale by one government, may be taxed by the other."

More recently the Court reexamined the question of taxing the gains of lessees of state or federal lands in *Helvering v. Producers' Corporation*, 303 U. S. 376 (1938). The Court recognized the distinction between a tax upon the state and a tax upon the lessee when it framed the issue before it thus (p. 384):

> "whether in a case where a tax is not laid upon the *leases* as such, or upon the *government's property* or interest, but is imposed upon the gains of the lessee, like that laid upon others engaged in similar business enterprises, there is in truth such a direct and substantial interference with the performance of the government's obligation as to require immunity for the lessee's income." (Emphasis supplied.)

The State does not suppose that it is contended that the federal government may tax the income the states realize from leases of lands containing saleable natural resources. Is the state to be burdened because as a matter of state policy it is thought more desirable to dispose of these resources as a continuous state activity? Or conversely, if the federal government chose to produce and sell the oil on Indian lands, could a state tax the sale thereof or income produced thereby?

The case at bar presents such a situation. Involved here is a federal tax upon the sale by the State of its natural resources. The incidence of the tax is directly upon the State. Without reviewing all of the facts contained in the statement, the State points out that the sale of these natural waters by the petitioners is not an isolated activity, but merely a small part of a larger program of conservation of natural resources, promotion of health and creation of recreation facilities.

The distinction, therefore, between the case at bar and the cases cited by the District Court and the Circuit

Court of Appeals is readily apparent. In *South Carolina* v. *United States*, 199 U. S. 437; *Ohio* v. *Helvering*, 292 U. S. 360; *Helvering* v. *Powers*, 293 U. S. 214; and *Allen* v. *Regents*, 304 U. S. 439, the respective state was not engaged in the disposition of its natural resources. In the *South Carolina* and *Ohio* cases, the states bought and sold liquor; in the *Powers* case the state merely took over the management of an existing railway; in the *Regents* case the state constructed two stadia seating about 30,000 people each for universities whose student bodies were about 2,000 each, and sold admissions (304 U. S. p. 450). The facts in each of those cases are significant as to why an exception was made to the general principle of immunity of state activities from direct burdens.

The State points out that in the *South Carolina* case, the source of all adverse authorities, one of the most powerful considerations was the Court's fear that if the liquor business were free from federal taxation, the states might enter other businesses and thus destroy a large source of federal revenue. The three other cases cited against the State are to similar effect.

That consideration is certainly not present in the case at bar. If this Court should hold that the State may sell its natural mineral waters free from federal tax, there is no need to fear that the State may exercise its police powers in other fields of activity and thus limit the sources of federal revenue. The number of natural resources is not large and thus the list of immune activities rather limited. Furthermore, with respect to the particular facts of the case at bar, it is to be noticed that the State did not acquire the springs at Saratoga to bottle and sell the waters. In fact, although the first legislation creating the board

known as "The Commissioners of the State Reservation at Saratoga Springs" gave it the power to sell the excess of mineral water not used on the premises (L. 1909, ch. 569, Sec. 5), it was not until 1930 that the successors of this original board exercised that power.

It was urged by the United States herein that the absence of profits or the fact that profits from the sale of waters are used to defray the expenses of the Reservation will not immunize the sales. The State similarly contends that the fact that profits *are* realized from the sales does not *deprive* them of their immunity. As the Court said in *Brush* v. *Commissioner*, 300 U. S. 352, 372-373 (1936):

> "If that service be governmental it does not become private because a charge is made for it, or a profit realized. A state, for example, constructs and operates a highway. It may, if it choose, exact compensation for its use from those who travel over it (see *Bingham* v. *Golden Eagle Lines*, 297 U. S. 626, 628); but this does not destroy the claim that the maintenance of the highway is a public and governmental function. The state or the city may exact a tuition charge for instruction in the public schools; but thereby the maintenance of the public schools does not cease to be a function of the government. The state exacts a fee for issuing a license or granting a permit; for recording a deed; for rendering a variety of services in the judicial department. Do these various services thereby lose their character as governmental functions? The federal Post Office Department charges for its services; but no one would question the fact that its operation calls into exercise a governmental function."

Again, it is to be noticed that on the facts of the case at bar the sale of these natural waters is not an isolated activity, but is related to a particular program of conservation, health, and recreation. It is recognized that the Court, in *Allen* v. *Regents*, was not persuaded to exempt football tickets from a federal tax because the proceeds

of the exhibition were used to finance a state educational program. But in that case a state was merely the collecting agency for the tax which was payable by the purchaser of the ticket, whereas here the tax is against a state itself. Mention is made of the larger program at Saratoga Springs, however, because it is only in connection with that program that the State decided to sell these waters. Thus, to grant immunity in the case at bar does not necessarily require immunity when a state engages in a wholesale disposition of its natural resources, unrelated to any particular public program.

The State sees no reason why the taxing power of the federal government will be seriously impaired if the sale of Saratoga mineral waters is free from tax. On the other hand, to hold this activity within the scope of the federal taxing power might seriously hamper the operation of the program of conservation, health and recreation at the Spa.

Conclusion

Upon the foregoing argument it is respectfully submitted that the judgments below should be reversed and the complaint dismissed.

Albany, September 7, 1944.

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Supreme Court of the United States

OCTOBER TERM, 1944

NO. [redacted] 5

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

THE UNITED STATES OF AMERICA

BRIEF FOR

SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY

Petitioners.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

NO. 83

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

THE UNITED STATES OF AMERICA

BRIEF FOR

SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY

I

Status of Petitioners Commission and Authority

The petitioners Saratoga Springs Commission and Saratoga Springs Authority are the governmental agencies of the State of New York charged with the development of the Saratoga Reservation and Cure for public health purposes according to the declared policy of the State. (R. 13)

The interests of these agencies are identical with those of the petitioner State of New York, although they appeared and answered herein by their local counsel, who join in the arguments submitted by the Attorney General and limit this memorandum to certain considerations which these petitioners desire to further emphasize.

Following the depletion of the natural mineral springs at Saratoga Springs through excessive pumping, (See Hathorn v. Natural Carbonic Gas Co. 194 N. Y. 326; People of the State of New York v. The New Yor' Carbonic Acid Gas Co. 196 N. Y. 421) the Legislature of the State of New York by Chapter 569 of the Laws of 1909, (R. 21) appropriated the sum of $600,000. for the use of a board to be appointed by the Governor under the name and style of the Commissioners of the State Reservation at Saratoga Springs, "to select and locate such lands in the Town of Saratoga Springs, in the County of Saratoga, and any rights, easements or interest upon or in any lands in said Town as it should deem proper and necessary to be taken, for the purpose of preserving the natural mineral springs in said Town of Saratoga Springs, and of restoring said springs to their former natural condition." The act further declared that the properties so acquired should "become and be the property of the State of New York." (Section 2) This act was amended by Chapters 394 and 469 of the Laws of 1911, and the purposes of the State more definitely defined. By Section 4 of Chapter 394 of the Laws of 1911, "promoting the resort to the said springs of the people of the State for health and other suitable use of the said reservation by the people, and of identifying, safeguarding and assuring the natural purity, qualities and repute of such waters and gases and for the purpose of providing the said waters to the people for drinking free of charge" were added to the purposes already mentioned. The Board, by Section 5, was authorized to prescribe the terms upon which any excess of mineral water and gas not used on said reservation should be sold or distributed, and was authorized to sell or dispose of such excess of water. The appropriation was increased to $950,000. By Chapter 252 of the Laws of 1914, a further appropriation of $235,000. was authorized. Acting under these various enactments, large properties and numerous mineral springs were acquired and became vested in the State of New York; bath houses were built and the water ulitized for drinking and bathing purposes. Bottling and distribution of bottled waters was

accomplished through a lease to a private corporation. By Chapter 295 of the Laws of 1916, the powers of the Board of Commissioners of the State Reservation at Saratoga Springs were transferred to the Conservation Commission.

There were amendments to the Conservation Law in respect to the reservation at Saratoga Springs by Chapters 204 and 468 of the Laws of 1917, and by Chapters 203 and 619 of the Laws of 1926. By Chapter 866 of the Laws of 1930, a temporary state commission to be known as the Saratoga Springs Commission, was created "for the purpose of ultimately developing the Saratoga Springs Reservation as a State health resort and spa, for the use of the public for balneological, therapeutic and other similar healthful purposes." This act also stated that "the development of such reservation for public health purposes is hereby declared a policy of the State in accordance with the recommendations of the commission appointed pursuant to the provisions of Chapter 668 of the Laws of 1929."

By Section 4 of this act, "jurisdiction, supervision, possession and control of all the lands, properties, property rights and easements, mineral springs, wells and all the other adjuncts constituting the Saratoga Springs Reservation now possessed and exercised by the Conservation Department, acting by or through the Division of Saratoga Springs Reservation" were transferred to the Commission for the term of seven years. The Commission was expressly authorized and empowered to negotiate with the Saratoga Springs Waters Corporation for the modification of its lease above referred to, and subsequently it acquired all of the rights of this corporation for the unexpired term of the lease. By Chapter 279 of the Laws of 1937, this commission was continued as a permanent commission, subject to the approval, supervision and control of the Conservation Commissioner, in the same manner as prescribed by law for the Division of Parks.

The Saratoga Springs Authority was created by Chap

ter 208 of the Laws of 1933, as a "body corporate and politic constituting a public benefit corporation." It was to continue only for a period of four years and thereafter until its liabilities have been met and its bonds have been paid in full, or such liabilities or bonds have otherwise been discharged. Upon its ceasing to exist, all its rights and properties shall pass to the State of New York. This corporation is created for the purpose and charged with the duty of development of the Saratoga Cure for public health purposes in accordance with the declaration contained in Chapter 866 of the Laws of 1930, that the development of the Saratoga Springs Reservation for public health purposes is a policy of the State in accordance with the recommendations of the commission appointed pursuant to the provisions of Chapter 668 of the Laws of 1929. The Authority was given broad powers including the right to maintain, construct and operate the cure defined by the act to mean "the property of the Authority devoted to the therapeutic use of mineral water for baths and drinking and to the bottling and sale thereof" etc., and to issue bonds secured by the revenues of the cure, etc. It was also authorized to lease from the Commission any portion of the State Reservation at Saratoga Springs "now owned by the State of New York or which may hereafter be acquired, with the approval of the Governor, for a term not exceeding ninety years, at a nominal or such other rental as may be determined," and the Saratoga Springs Commission was authorized and empowered to enter into such lease, and did thereafter grant a lease of all of its properties to the Authority, which is still in existence, its bonded indebtedness not having been paid, and operating the Saratoga cure, as provided in said act.

The defendants are not engaged in any commercial enterprise for profit (R. 20), but on the contrary, are carrying out the declared policy of the State of New York to develop the Saratoga Springs Reservation as a State health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes.

In this enterprise, the State of New York has appropriated upwards of $5,600,000. for the purchase and improvement of the reservation property, all of which is owned by and vested in the State of New York and not in the Commission or Authority. (R. 30) This ownership includes mineral springs from which water is bottled and sold by the State as one method of distribution. The tax in question is on the property of and against the State. It is direct and not remote in its operation and effect, and is clearly in conflict with the state's immunity from taxation by the federal government.

II

The petitioners claim immunity from tax on sales of bottled waters incidental to and in furtherance of the State's health policy.

The trial court denied the claimed immunity upon the ground that the petitioners were engaged in a business enterprise conducted by the State for gain (R. 25). The affirming court accepted this basis among others (R. 36).

This basis lacks factual support in this case. The mineral waters at Saratoga are unique in their natural composition (R. 12). Those upon which the taxes in question were levied and which were bottled and sold in their natural state were Hathorn, a laxative water, Coesa, a diuretic water, and Geyser, a digestive water. A plain water known as State Seal, of high chemical and vegetable purity, used very largely in various State institutions and offices, was also sold in small amount (R. 14). These waters were in no sense a commercial product. Except State Seal, these waters are not suitable for indiscriminate beverage use, and cannot be mixed with fruit juices or alcoholic beverages (R. 14). It nowhere appears in the record and it is not a fact, that any of these natural mineral waters

are produced or sold by any other person or corporation. They are not a commodity capable of manufacture or production by anyone, but are a natural resource of the State, of limited territorial extent and practical State monopoly. No other natural or manufactured waters have exactly the same chemical content or the same State guarantee as to purity (R. 12, 14).

The Circuit Court of Appeals not only misconstrued these facts into what it characterized as "a common private enterprise," but found no distinction between the State's sales of these natural and unique waters in the interest of its health and conservation policy, and the traffic in alcoholic beverages held subject to a license tax in the South Carolina and Ohio cases. (199 U. S. 427; 292 U. S. 360).

The distribution of water for a great variety of purposes—ranging from ordinary agricultural, domestic and sanitary uses to the preservation of health and life—has been recognized as distinctly a governmental function.

> Brush v. Commissioner of Internal Revenue 300 U. S. 352, 366.

Neither the governmental function nor business enterprise test has escaped criticism. (See Mr. Justice Black's cogent remarks in Helvering v. Gerhardt, 304 U. S. 405, 426). Public opinion and political science now admit a much wider scope for essential governmental operations than the generation of Mr. Herbert Spenser would have approved. Tax immunity is as essential to the proper exercise of new functions as of old.

The business enterprise test standing alone has not been productive of much result until this case. In the cases where it has been heretofore invoked, it has either been found inapplicable, as in Indian Motor Cycle Co. v. U. S., 283 U. S. 570, or the tax has been capable of being sustained

upon some other basis as well, as in Board of Trustees of University of Ill. v. U. S., 289 U. S. 48, involving a duty under foreign commerce over which the United States had plenary power, or the South Carolina and Ohio liquor cases involving a license fee and not a tax on property, or Allen v. Regents, 304 U. S. 439, where the State was a mere collector. This test appears never to have been sufficiently virile to sustain a direct tax against a state's property or property transactions.

The court below did not rest entirely on the business enterprise test but sought a further or ultimate basis in the need of the state activity to maintain the states as they exist (R. 36). This is equally indefinite and not only involves the conflict of doctrine already mentioned but the further uncertainty as to the degree of danger and the effect of the tax from its amount which the court seems to have felt to be unstable considerations in Indian Motor Cycle Co. v. U. S., 283 U. S. 570.

The conditions which this court seems to have finally adopted as necessary to validity where states have attempted to tax the Federal Government or its instrumentalities, i.e., freedom from discrimination against transactions with the government and freedom from direct imposition upon the property and the instrumentalities of the government (See dissenting opinion of Mr. Justice Frankfurter in United States v. Allegheny County, Pa., 64 Supreme Court Reporter 908, 919) seems equally applicable to Federal efforts to burden the states.

The tax was improperly imposed upon the petitioners not only because it was a direct tax contrary to the conditions above referred to but also because in distributing its medicinal waters the State was not engaged in business within the meaning of the business enterprise test, but was exercising a recognized governmental function.

The judgment should be reversed and the complaint dismissed.

All of which is respectfully submitted.

Dated at Saratoga Springs, N. Y., Oct. 7, 1944.

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Supreme Court of the United States

OCTOBER TERM, 1945

No. 5

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

UNITED STATES OF AMERICA.

BRIEF ON REARGUMENT, FOR THE STATE OF NEW YORK, PETITIONER

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UNITED STATES OF AMERICA.

BRIEF ON REARGUMENT, FOR THE STATE OF NEW YORK, PETITIONER

Introductory

Certiorari was granted by this Court on June 12, 1944, and the case was No. 83 on the calendar for the October 1944 Term. It was argued on December 7 and 8, 1944. Reargument was directed on June 18, 1945, and on October 8, 1945, the Court invited attention to the following questions:

> "1. May Congress constitutionally include for taxation in a generally applicable taxing act any state property or activity or the income derived by the state from them, or any other source, so long as the tax does not discriminate against the state, or so long as the tax is not laid on the interest taxed, merely because it is that of a state—and if income of a private person from a like source may be constitutionally taxed?
>
> "2. To what extent may a state, by enlarging its property ownership or its activities, withdraw from

of a rule which would permit inclusion of state and municipal activities within the scope of any and all non-discriminatory federal taxing statutes, merely because a private person would be taxable under the same circumstances, is wholly unjustified and unfair. Such a rule would defeat the reasonable expectations of those who purchased state and municipal bonds in good faith, and would seriously handicap the States in their legitimate activities.

Outline of Argument

I. A tax which is imposed directly upon state property or a state activity or the income therefrom is unconstitutional, even though non-discriminatory. (Answering question 1 above.)

II. The disposal by a state of its natural resources, and particularly of water, is a governmental activity constitutionally immune from federal taxation. (Supplementing our original brief on this point.)

III. The fact that a state, in enlarging its property ownership or its activities, enters a field which would be taxable as a private enterprise, does not constitute a ground for denying it tax immunity. (Answering question 2 above.)

(1) The States should be given the same freedom from tax burdens in enlarging their activities within the fields reserved to the States that the Federal Government has within the powers delegated to it.

(2) The general rule is, and should continue to be, that the immunities of the States and of the Federal Government are reciprocal.

(3) No previous case has sustained a federal tax upon a public service rendered by a state or political subdivision.

POINT I

A tax which is imposed directly upon state property or a state activity or the income therefrom is unconstitutional even though non-discriminatory.

The general tenor of the decisions of this Court over more than a century of time is, that any tax imposed by one government directly on another is *prima facie* a violation of the fundamental principle of intergovernmental tax immunity. The cases where special circumstances have led the Court to uphold a tax against a state will be treated in Point III of this brief. But the fact that a tax is non-discriminatory has never been considered in itself a justification for the tax.

The decision in the first case on intergovernmental immunity (*McCulloch* v. *Maryland*, 4 Wheat. 316) did not turn on the fact that the tax involved was discriminatory, although the tax was in fact confined to banks not chartered by the State Legislature (p. 320). Chief Justice Marshall stated (pp. 436-437):

> "This is a tax on the operations of the bank, and is, consequently, a tax on the operation of an instrument employed by the government of the Union to carry its powers into execution. Such a tax must be unconstitutional."

The next case on the subject involved a nondiscriminatory tax. In *Weston* v. *City Council of Charleston*, 2 Pet. 449, Chief Justice Marshall struck down a local tax as applied to stock in the Bank of United States because "it bore directly upon the contract evidenced by the stock" and because "if the right to impose the tax exists, it is a right which in its nature acknowledges no limits" (p. 466). See *Helvering* v. *Gerhardt*, 304 U. S. 405, 413, where Mr. Justice, now Chief Justice, Stone recognized the *Weston* case as establishing the rule "that federal instrumentalities are similarly immune from nondiscriminatory state taxation."

The correlative immunity of the states found expression in *Veazie Bank* v. *Fenno*, 8 Wall. 533, which upheld a federal tax on notes issued by a bank chartered by the State of Maine, but not sustaining any relation to the State as a financial agent (p. 535), the Court stating (p. 547):

> "It may be admitted that the reserved rights of the States, such as the right to pass laws, to give effect to laws through executive action, to administer justice through the courts, *and to employ all necessary agencies for legitimate purposes of State government*,* are not proper subjects of the taxing power of Congress."

We have already quoted the language of Mr. Justice Nelson in *Collector* v. *Day*, 11 Wall. 113, 127 (main brief, p. 7), that the exemption of state instrumentalities from federal taxes "rests upon necessary implication, and is upheld by the great law of self-preservation." The tax involved in *Collector* v. *Day* was the Civil War income tax on the income "of every person residing in the United States." While it has now been held that a tax on salaries is not a direct burden on the government which pays the salaries, *Collector* v. *Day* still stands for the principle that any direct burden upon a state function, even though not discriminatory, is unconstitutional.

It was a non-discriminatory federal tax upon the bonds of transportation companies which was held invalid as to the City of Baltimore in *United States* v. *Railroad Co.*, 17 Wall. 322. The Court there stated (p. 327):

> "The power of taxation by the Federal government upon the subjects and in the manner prescribed by the act we are considering, is undoubted. There are, however, certain departments which are excepted from the general power. The right of the States to administer their own affairs through their legislative, executive and judicial departments, in their

* Italics throughout this brief are inserted by counsel, unless otherwise noted.

> own manner through their own agencies, is conceded by the uniform decisions of this court and by the practice of the Federal government from its organization. This carries with it an exemption of those agencies and instruments, from the taxing power of the Federal government."

The argument was made there, in substance, that an investment in a railroad was not a strictly governmental purpose, just as it is argued here that the selling of bottled water is not a strictly governmental activity, but the Court held that the legislative grant of power to invest in such bonds "was conferred because its exercise concerned the public and to benefit that public" (p. 331) and concluded, "We are clear in the opinion that the present transaction is within the range of the municipal duties of the city, and that the tax cannot be collected": (p. 333).

Lands of the United States were held exempt from state taxation in *Van Brocklin* v. *Tennessee*, 117 U. S. 151. The lands had been acquired for non-payment of direct taxes laid by Congress, and were afterwards sold by the United States for a sum larger than the original tax and penalties. Neither the fact that the tax was non-discriminatory nor the contention that Tennessee had never ceded exclusive jurisdiction over the land to the United States, availed to save the tax.

It was again a non-discriminatory income tax which was held invalid as to state and municipal securities in *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429. The opinion of Chief Justice Fuller stated (p. 586):

> "Applying this language* to municipal securities, it is obvious that taxation on the interest therefrom would operate on the power to borrow before it is exercised, and would have a sensible influence on the

* The reference is to Chief Justice Marshall's opinion in *Weston* v. *Charleston, supra* (2 Pet. 449, 468), holding that a state tax could not be applied to stock in the Bank of the United States.

> contract, and that *the tax in question is a tax on the power of the states and their instrumentalities to borrow money, and consequently repugnant to the Constitution.*"

All the Justices agreed on this phase of the case. Mr. Justice Field's opinion quoted (p. 603) *United States* v. *Railroad Co.*, 17 Wall. 322, 327, that the power of the states to administer their own agencies "carries with it an exemption of those agencies and instruments from the taxing power of the Federal government." Mr. Justice White stated (p. 652) that "In regard to the right to include in an income tax the interest upon the bonds of municipal corporations, I think the decisions of this court, holding that the Federal government is without power to tax the agencies of the state government, embrace such bonds, and that this settled line of authority is conclusive upon my judgment here." Mr. Justice Harlan stated (p. 653) that "The instrumentalities employed by the States in execution of their powers are not subjects of taxation by the general government, any more than the instrumentalities of the United States are the subjects of taxation by the States." The opinions on reargument adhered to this same view (158 U. S. 601 at 630, 665-666, 693).

State and federal immunities were considered comparable in *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, which sustained a federal income tax upon the compensation of a consulting engineer engaged by a state. The Court, by Mr. Justice Stone, stated (pp. 522-23):

> "Just what instrumentalities of either a state or the federal government are exempt from taxation by the other cannot be stated in terms of universal application. But this Court has repeatedly held that those agencies through which either government immediately and directly exercises its sovereign powers, are immune from the taxing power of the other. * * * it rests on the conviction that each government, in

order that it may administer its affairs within its own sphere, must be left free from undue interference by the other."

When this Court in *Willcuts* v. *Bunn*, 282 U. S. 216, sustained an income tax upon profits made from the sale of municipal bonds, it based its decision not alone on the fact that the tax was non-discriminatory, but treated as decisive the fact that a tax on such a transaction did not directly burden the state, and that any injury to the state's borrowing power was imaginary and negligible (pp. 229-234). Chief Justice Hughes stated (pp. 224-25):

> "The well-established principle is invoked that a tax upon the instrumentalities of the States is forbidden by the Federal Constitution, the exemption resting upon necessary implication in order effectively to maintain our dual system of government.
>
> * * * * * *
>
> The power to tax is no less essential than the power to borrow money, and, in preserving the latter, it is not necessary to cripple the former by extending the constitutional exemption from taxation to those subjects which fall within the general application of non-discriminatory laws, *and* where no direct burden is laid upon the governmental instrumentality, and there is only a remote, if any, influence upon the exercise of the functions of government."

A non-discriminatory tax was before this Court in *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, involving an excise tax which the Court found was levied on the sale of motorcycles. It was there held that the tax could not be imposed on the sale of a motorcycle to a municipal corporation for use in its police service. Mr. Justice Van Devanter declared (pp. 575-76):

> "It is an established principle of our constitutional system of dual government that the instrumentalities, means and operations whereby the United States exercises its governmental powers are exempt from taxation by the States, and that the instrumentalities, means and operations whereby the States exert the

governmental powers belonging to them are equally exempt from taxation by the United States. This principle is implied from the independence of the national and state governments within their respective spheres and from the provisions of the Constitution which look to the maintenance of the dual system. *Collector* v. *Day*, 11 Wall. 113, 125, 127; *Willcuts* v. *Bunn*, 282 U. S. 216, 224-225. Where the principle applies it is not affected by the amount of the particular tax or the extent of the resulting interference, but is absolute. *McCulloch* v. *Maryland*, 4 Wheat. 316, 430; *United States* v. *Baltimore & Ohio R. Co.*, 17 Wall. 322, 327; *Johnson* v. *Maryland*, 254 U. S. 51, 55-56; *Gillespie* v. *Oklahoma*, 257 U. S. 501, 505; *Crandall* v. *Nevada*, 6 Wall. 35, 44-46."

A non-discriminatory tax must still meet the test that it is not imposed directly upon a state or municipal government. The recent redefinition of the scope of immunity, permitting taxes which may indirectly burden a government, has no tendency to indicate that a non-discriminatory tax laid directly upon a State or municipal activity will be sustained.

It seems to be accepted that the present case involves a direct tax upon the state. The United States does not now and never has argued against that proposition. Federal taxes which are a direct burden upon state activities are not valid simply because they do not discriminate against the state and are not laid on the interest taxed merely because it is that of a state.

The necessity that a tax not only be non-discriminatory but that it not be laid directly upon the state, was repeated in *Helvering* v. *Mountain Producers Corporation*, 303 U. S. 376, which upheld an income tax on a lessee of state oil lands. The question which Chief Justice Hughes considered vital in the *Mountain Producers* case was—

"whether in a case where the tax is not laid upon the leases as such, or upon the government's prop

erty or interest, but is imposed upon the gains of the lessee, like that laid upon others engaged in similar business enterprises, there is in truth such a direct and substantial interference with the performance of the government's obligation as to require immunity for the lessee's income" (p. 384).

The fact that the tax was not directly upon the state was the reason for upholding it. The Court stated (p. 387):

> "In the instant case, we find no ground for concluding that the tax upon the profits of Wyoming Associated derived under its lease from the State constituted any direct and substantial interference with the execution of the trust which the State has assumed."

When this Court held in *Helvering* v. *Gerhardt*, 304 U. S. 405, that the Federal Government might tax the income of the employees of state agencies, it did not find that the non-discriminatory character of the income tax was sufficient to remove the case from state immunity, but it pointed out the lack of any direct burden upon the state, saying (p. 421):

> "The effect of the immunity if allowed would be to relieve respondents of their duty of financial support to the national government, in order to secure to the state a theoretical advantage so speculative in its character and measurement as to be unsubstantial. A tax immunity devised for protection of the states as governmental entities cannot be pressed so far.
>
> "The fact that the expenses of the state government might be lessened if all those who deal with it were tax exempt was not thought to be an adequate basis for tax immunity in *Metcalf & Eddy* v. *Mitchell, supra*, in *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279, in *Burnet* v. *Jergins Trust*, 288 U. S. 508; or in *Helvering* v. *Mountain Producers Corp.*, 303 U. S. 376. When immunity is claimed from a tax laid on private persons, it must clearly appear that the burden upon the state function is actual and substantial, not conjectural. *Willcuts* v. *Bunn, supra*, 231. The extent to which salaries in business or professions whose standards of compensation are otherwise fixed by competitive con-

ditions may be affected by the immunity of state employees from income tax is to a high degree conjectural."

It is true that the Court has observed in cases where it has permitted a tax against state agencies that the tax was non-discriminatory (See, *e. g., Allen* v. *Regents,* 304 U. S. at 452). But it would be a *non sequitur* to assert that every non-discriminatory tax is valid.

In determining the extent of federal immunity from state taxation this Court has adhered to the rule that a tax directly upon a governmental activity is invalid even though non-discriminatory. *Federal Land Bank* v. *Crosland,* 261 U. S. 374; *Maricopa County* v. *Valley National Bank,* 318 U. S. 357; *Mayo* v. *United States,* 319 U. S. 441; *City of Cleveland* v. *United States,* 323 U. S. 329; cf. *Smith* v. *Davis,* 323 U. S. 111.

Mr. Justice Jackson has summarized the Court's decisions by stating that:

> "The distinction between taxation of private interests and taxation of governmental interests, although sometimes difficult to define, is fundamental in application of the immunity doctrine as developed in this country."
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> *United States* v. *Allegheny County,* 322 U. S. 174, 186.

See also T. R. Powell, *The Remnant of Intergovernmental Tax Immunities,* 58 Harv. L. Rev. 757, 786-87.

Mr. Justice Frankfurter, who had earlier called attention to the unjustified extension of the immunity doctrine to subjects not directly affecting the State or Federal Governments,* has described the present basis of the Federal Government's immunity in the following terms:

> "The basis of the doctrine was shifted from that of an argumentative financial burden to the Federal Govern-

* Frankfurter, *Mr. Justice Holmes and the Supreme Court* (1938) 85. These lectures were given in April, 1938, and doubtless prepared some time before this Court's opinions in *Helvering* v. *Gerhardt, supra* (304 U. S. 405), decided May 23, 1938.

ment to that of freedom from discrimination against transactions with the Government *and freedom from direct impositions upon the property and the instrumentalities of the Government.*"

United States v. *Allegheny County*, 322 U. S. 174, 196.

It may be suggested that the trend of the Court to approve taxes which only indirectly burden the state or federal governments should lead also to a relaxation of the rules against direct burdens. Logic seems to point in the opposite direction. The right to impose taxes upon persons who deal with or work for the state or federal governments removes the danger of serious restriction upon the taxing power, and thus removes one of the main reasons which led this Court to make exceptions to the doctrine of state immunity in *South Carolina* v. *United States*, 199 U. S. 437.

The exemption of state or federal employees from general income taxes was objectionable as tending to create a "privileged class of taxpayers" (*Helvering* v. *Gerhardt*, 304 U. S. 405, at 416). Recognition of immunity from taxes laid directly upon a state activity has no such effect. On the contrary, the tendency if such immunity were denied would be to discourage state pioneering in new activities, as we shall more fully outline in a later Point.

A ruling under which all non-discriminatory taxes would be approved does not even have the advantage of simplicity. There are indications in the cases, however, that it is not always easy to tell what is a discriminatory tax. *Gregg Dyeing Co.* v. *Query*, 286 U. S. 472; *Cf. Northwest Airlines, Inc.* v. *Minnesota*, 322 U. S. 292. It might be considered discriminatory as against the states to tax a state activity in a field where the Federal Government is also operating and is free from tax; regardless of the manner in which private business is treated, the collection of a tax from a state activity and the exemption of a comparable federal activity would seem to be the equivalent

to laying a tax on the activity merely because it is that of a state. In any event, a fancied simplicity of application should be a less important consideration in adopting a standard of immunity than that of consistency with prior rulings of this Court, or that of its practical effect upon the States.

Taxes which are imposed directly upon a state activity tend to discourage the state from embarking on that activity. The long-established rulings of this Court forbid such direct burdens, and ought not to be overruled.

The principle of intergovernmental tax immunity is based on implication from the existence of state and federal governments within the same territory. But even the limited immunity suggested by this Court's first question—an immunity from taxes discriminating against state activity—must rest on implication rather than on express language. We know of no reason which would compel the adoption at this late date of an interpretation which would so limit the immunity of the States. On the contrary, we shall show that such a doctrine would have serious consequences to our state and local governments. In the face of repeated statements by this Court that immunity extends to non-discriminatory taxes, there is no justification for now excluding all such taxes from the scope of the immunity.

POINT II

The disposal by a state of its natural resources, and particularly of water, is a governmental activity constitutionally immune from federal taxation.

This Court has recognized as legitimate fields of state activity, entitled to constitutional immunity, both the exploitation of natural resources and the development of water supply.

State exploitation of natural resources is a governmental activity.

Burnet v. *Coronado Oil & Gas Co.*, 285 U. S. 393, stands for two propositions: First, that an oil lease covering state-owned lands is an instrumentality of the state in the exercise of a governmental function, and second, that application of the federal income tax to the income derived from the lease by the lessee is a direct burden upon the state government. The second proposition has now been repudiated (*Helvering* v. *Mountain Producers Corp.*, 303 U. S. 376) on the ground that the tax was not a direct and substantial burden upon the state. But the first proposition, that the activity was governmental, has not been disturbed. The Court said on this point (285 U. S. at 400):

> "When Oklahoma undertook to lease her public lands for the benefit of the public schools she exercised a function strictly governmental in character. Consequently, *South Carolina* v. *United States*, 199 U. S. 437, much relied upon, is not in point."

The Oklahoma Legislature had directed payment of the proceeds of the oil leases into the school fund (285 U. S. at 398) to provide free public education. New York utilizes the proceeds of sale of Saratoga Spring waters for payment of the current expenses of the Saratoga Springs Reservation, so that it may provide free treatments for needy and ailing citizens at Saratoga Springs (R. 17-19).

The acts of the State of New York, in bottling and selling the mineral waters of Saratoga Springs for the benefit of the public health, are no less governmental in character than the actions of Oklahoma in leasing its oil lands for the benefit of public education (see State's original brief, pp. 12-13).

Another example illustrates the anomaly which might result from denial of immunity for a state's disposal of natural resources. The National Government and State

Governments own forests, and presumably in years to come will engage in harvesting timber even more extensively than at present. It is quite conceivable that each may impose an excise tax measured by all severances of timber within the respective taxing jurisdiction. To distinguish between the two cases upon the ground that lumbering operations of the Federal Government are necessarily "governmental" and hence immune, but that such operations of a state are "proprietary" and taxable, will not be a satisfactory contribution to clarity of constitutional doctrine.

Nor should the circumstance that the mineral springs at Saratoga were at one time in private hands alter the governmental character of their present operation. The reason why the state reacquired the waters at Saratoga was that private operation had proved wasteful and detrimental to the conservation of those waters in the interest of public health (R. 12-13).* States have been held to have a legitimate interest in the efficient use of their natural resources *Champlin Refining Co.* v. *Corporation Commission,* 286 U. S. 210; *cf. Lindsley* v. *Natural Carbonic Gas Co.,* 220 U. S. 61.

The Court in *Ashwander* v. *Tennessee Valley Authority,* 297 U. S. 288, 330-40, construed broadly the power of the Federal Government to dispose of property it had ac-

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* Another reason may well have been the necessity for strict control of the bottling, in order to preserve the virtues of the waters. The process used in bottling was worked out by State employees before the lease to Saratoga State Waters Corporation was made in 1920. See 1932 Annual Report of Saratoga Springs Commission, 1933 N. Y. Leg. Doc. No. 96, p. 19. The process includes filling the empty bottle with carbon dioxide before waters are introduced into it, and storing it to let any sediment settle. 1937 Annual Report, p. 13. The process is an expensive one, and the Saratoga waters are substantially the only waters in the eastern United States which are bottled in their natural state (1938 Annual Report, p. 7).

quired, and left no doubt that this is a governmental power. The same should be true when a state disposes of its property.

The extent of the state's power in the development and use of its natural resources should not be diminished by the fact that it had been necessary to correct the mistake of a previous commission which had permitted those resources to pass temporarily into private hands.* It may be pointed out, moreover, that the lands of the Federal Government which were held constitutionally tax exempt in *Van Brocklin* v. *Tennessee,* 117 U. S. 151, were lands which had once been in private hands, and the machinery which was given constitutional immunity in *United States* v. *Allegheny County,* 322 U. S. 174, had doubtless been bought from a private manufacturer.

The supply and conservation of water is a governmental activity

The state's immunity in the present case does not rest alone upon the general governmental character of any disposal of a public natural resource. Water is peculiarly the subject matter of governmental activity, as this Court has expressly recognized.

In *Brush* v. *Commissioner,* 300 U. S. 352, the Court reviewed the history of water supply, and held that an employee of the Bureau of Water Supply of the City of New York was performing a governmental function, and was therefore immune from federal income tax. (As in other salary cases, we consider it clear that the determination of the immune character of the activity survives even though a tax on salaries is no longer con-

* The lease of the bottling privileges by the Saratoga Springs Reservation Commission had met with prompt and strong opposition from those who considered that the distribution of the waters should not be primarily a trade undertaking but a public health undertaking. Lasker, *The Wand of Manitou,* 44 The Survey 329, 333 (1920).

sidered a direct burden on the activity.). The Court there stated:

> "The public interest in the conservation and distribution of water for a great variety of purposes—ranging from ordinary agricultural, domestic and sanitary uses, to the preservation of health and of life itself—is obvious and well settled" (p. 366).
>
> "We conclude that the acquisition and distribution of a supply of water for the needs of the modern city involve the exercise of essential governmental functions, and this conclusion is fortified by a consideration of the public uses to which the water is put" (p. 370).

The question whether the activity was profitable was not considered decisive, the Court stating:

> "If that service be governmental it does not become private because a charge is made for it, or a profit realized" (300 U. S. at 372).

Likewise, the fact that Army post exchanges operate at a profit has not been considered a sufficient reason for denying that they are essential for the performance of governmental functions. *Standard Oil Co.* v. *Johnson*, 316 U. S. 481.

Although the sale of water from Saratoga Springs results in some profit, when computed without depreciation or other capital charges (R. 18), the annual operating receipts of the reservation as a whole have never been sufficient to meet its expenses (R. 20).

The fact that the water involved in the present case is sold in bottles instead of being distributed in pipes, or that it is purchased on recommendation of physicians (R. 14) instead of being used indiscriminately, should not serve to differentiate the cases or obscure the fact that the activity is undertaken for the governmental purpose of promoting the public health and not for purely commercial or profit-making reasons.

The use which is made of water distributed by the government should not affect the governmental character of the distribution. Water from a municipal waterworks is commonly sold to private industry as well as to domestic consumers. But any distribution of water by the state or a municipality is made in response to the genuine public interest in the subject matter.

Nor does the fact that part of the water is sold outside New York State (R. 15) affect the case. The Government has not sought to differentiate between sales to New York residents and sales outside. Just as State universities are open on special terms to non-residents, the health-giving waters of Saratoga Springs may be made available to anyone who wishes them, without discrimination based on residence.

Public development of the waters at Saratoga is merely another example of the long-established policy of New York, expressed by Governors of both political persuasions, that water resources should be kept in public ownership. As Governor Charles Evans Hughes put it:

> "* * * In the light of exact information, a proper policy with reference to the development and control of water powers should be established in order that these important sources of our prosperity may be held to the utmost extent possible for the benefit of all the people." Public Papers of Governor Hughes 1908, p. 33.

See also Public Papers of Governor Martin H. Glynn 1914, pages 1209-10; Public Papers of Governor Alfred E. Smith 1920, page 337; Public Papers of Governor Franklin D. Roosevelt 1929, page 13; Public Papers of Governor Thomas E. Dewey 1943, page 22.

Cf. *Kaukauna Water Power Co.* v. *Green Bay Canal Co.*, 142 U. S. 254.

The states always retain a substantial "reserve power" over their natural waters, even after conveyances to private

interests. *Cf. Illinois Central R. R. Co.* v. *Illinois,* 146 U. S. 387; *Coxe* v. *State,* 144 N. Y. 396; *Matter of Niagara Falls Power Co.* v. *Water Power and Control Commission,* 267 N. Y. 265, 276.

The public interest in water resources within the State was a ground for special treatment of a New Jersey statute forbidding exportation of water. *Hudson Co. Water Co.* v. *McCarter,* 209 U. S. 349. The Court in that case permitted a prohibition against sale of water to non-residents, although such a distinction between citizens of different States would not have been permitted with respect to other types of property. *Cf. Pennsylvania* v. *West Virginia,* 262 U. S. 553.

No fancied similarity between the uses of whisky and of water should be permitted to obscure the fact that the State of New York is here engaged in a legitimate governmental activity which is entitled to protection from all direct tax burdens by any other sovereignty.

We are not unaware that a distinguished commentator, impressed by the decision in *South Carolina* v. *United States,* 199 U. S. 437, has stated concerning the case now *sub judice* that, "It will, however, occasion surprise if the Supreme Court should find a constitutional immunity for state furnished mineral water that it does not find for state furnished alcoholic spirits". T. R. Powell, *The Remnant of Intergovernmental Tax Immunities,* 58 Harv. L. Rev. 757, 794n. We might reply in the same vein that it would occasion surprise if any one made the mistake of mixing the laxative or diuretic waters of Saratoga Springs with whisky to form a highball. The waters are valued primarily for their medicinal virtues (R. 12, 14) and would be distasteful as a beverage component.* The language,

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* "they are not suitable for indiscriminate beverage use and cannot be mixed with fruit juices or alcoholic beverages" (Stipulation of Facts, par. 13—R. 14).

moreover, disregards the differences which this Court has already recognized in the *Brush* case, between the functions which a state subserves in distributing whisky and those which it subserves in distributing water.

The extent to which the State's development at Saratoga Springs subserves vital public interests may be seen from examination of the report submitted to the Legislature by the special Commission appointed in 1929 (1930 N. Y. Leg. Doc. No. 70—hereinafter called "Report"). This Commission, of which Bernard M. Baruch was chairman, reported that

> "the Commission and its expert advisers alike are convinced that an institution may be built up at Saratoga for the effective treatment of the chronically ill and those in danger of becoming so, especially those suffering from cardiac, vascular and circulatory ailments—ailments whose victims in the United States now number more than 235,000 each year, the greatest toll taken by any one group of diseases, and for whose treatment, it is agreed, the waters at Saratoga have great virtue." (Report, p. 5).

The Commission considered that it was "most necessary" that control of all use of the waters be placed under the State (Report, p. 9).

The analysis of comparable spas of the eastern United States (Report, pp. 51-66) shows that the development by New York State at Saratoga is not unique as a public venture, and that any contrary implications in the stipulation of facts (par. 20, R. 19) should not be relied upon.

The Report shows that the forty-four springs at Hot Springs, Arkansas have been the property of the United States Government for over a century, having been set aside as a national reservation in 1832, and made a national park, under the Department of the Interior, in 1921 (Report, p. 52). The bath houses at Hot Springs pay an annual fee for water, which is "piped direct from the

springs, the entire system of distribution being in the hands of the Government" (Report, p. 53).

The Report also shows that Berkeley Springs, West Virginia, is owned by the State, having been ceded to the Colony of Virginia by Lord Fairfax about the time of the French and Indian War (Report, p. 64); and that the Big Horn Hot Springs at Thermopolis, Wyoming, have been operated as a State reserve since 1897, when they were ceded to the State by the United States Government (Report, p. 65).

During the very time that the Federal Government has been disputing the governmental character of the State's activities at Saratoga Springs, a federal agency (the United States Veterans' Administration) has taken over one of the bath houses on the Saratoga Springs Reservation, and since February 1, 1943 it has been used "for administering the natural mineral water treatments to cardiac, arthritic and convalescent cases". New York Legislative Manual (1944) 553. So we have the strange situation here of two governments jointly using a single property, and the one claiming that, while its own use is admittedly governmental, it is entitled to tax the other on the theory that its activities are not governmental.

POINT III

The fact that a state, in enlarging its property or activities, enters a field which would be taxable as a private enterprise, does not constitute a ground for denying tax immunity.

The limitation upon the general principle of immunity is to be found at the exact point where it collides with and is outweighed by a competing principle. A state by enlarging its property ownership or its activities may "withdraw" from the reach of the federal taxing power

property and income which are normally subject to federal taxation when owned and received by private persons, to the point and only to the point, where the impropriety of one sovereign taxing another without its consent becomes outweighed by some competing constitutional principle of exigent federal interest.

Where the need of preserving federal revenue is the only competing principle, it is our view that the state's immunity should control, at least until there is an actual danger of serious impairment of the federal revenue.

There is nothing novel or unduly burdensome in this answer to the present question. In *Thomas* v. *Collins*, 323 U. S. 516, 544, Mr. Justice Jackson said: "As frequently is the case, this controversy is determined as soon as it is decided which of two well-established, but at times overlapping, constitutional principles will be applied to it." Mr. Justice Holmes stated the same thought in *Irwin* v. *Gavit*, 268 U. S. 161, 168: "Neither are we troubled by the question where to draw the line. That is the question in pretty much everything worth arguing in the law."

Both the state and federal governments from time to time own property or engage in activities which would be taxable in the hands of a private person. This fact in itself does not constitute a basis for denying immunity.

In *United States* v. *Railroad Company*, 17 Wall. 322, the question was the right to levy a withholding tax on the interest on bonds of the Baltimore & Ohio Railroad, owned by a municipal corporation. Clearly the interest from such bonds would have been taxable if they were in the hands of a private person. But that fact was not considered as justifying a denial of immunity or even an examination into the propriety of the investment. See 17 Wall. at 330-31.

The second question propounded by this Court on October 8th, relating to the "withdrawal" from federal tax-

ing power of property and income which would be subject to that power when owned or received by private persons, refers to "*United States* v. *California*, 297 U. S. 175, 184, 185, and cases cited."

We do not read *United States* v. *California* as holding that a state's venture into a field partly occupied by private enterprise necessarily subjects the state to tax. The issue in the case was the liability of the State of California for a statutory penalty for violation of the Federal Safety Appliance Act in the operation of a state-owned railroad serving the San Francisco Harbor. It was held that the claim of immunity should be denied. On the other hand, in a later case the same state's raisin marketing program was held immune from the Sherman Act, the test being stated as, "accommodation of the state and national interests involved." *Parker* v. *Brown*, 317 U. S. 341, 362. We suppose the test in the earlier case, likewise involving the relationship between the state's police power and the power of Congress under the commerce clause, to have been not substantially different. With respect to the governmental nature of the state activity involved in the earlier case of the harbor railroad the Court stated (297 U. S. at p. 183):

> "Despite reliance upon the point both by the government and the state, we think it unimportant to say whether the state conducts its railroad in its 'sovereign' or in its 'private' capacity. That in operating its railroad it is acting within a power reserved to the states cannot be doubted. See *Puget Sound Power & Light Co.* v. *Seattle*, 291 U. S. 619, 624; *Green* v. *Frazier*, 253 U. S. 233; *Jones* v. *Portland*, 245 U. S. 217."

The Court said of the state's reliance on tax immunity cases in connection with an interstate commerce issue that the analogy was "not illuminating" (p. 184). We shall show at a later point that the cases which the Court cited in connection with intergovernmental immunity are

consistent with the test which we have suggested in this brief. For the present it is sufficient to observe that the Court, after discussing the restrictions upon the federal taxing power, stated, "but there is no such limitation upon the plenary power to regulate commerce" (p. 185).

The case of *United States* v. *California*, in the emphasis it placed upon the commerce clause, is similar to *Veazie Bank* v. *Fenno*, 8 Wall. 533, where like emphasis was placed upon the currency power (pp. 548-549), or *Board of Trustees* v. *United States*, 289 U. S. 48, which held a state subject to the tariff act as an exercise of Congress' power "to regulate commerce with foreign nations" (p. 56). These cases are examples of specific federal regulatory powers which were held preponderant, but they do not prove that the general federal power of taxation for revenue, which has always been held subject to implied limitations in intergovernmental relations, should now be considered necessarily and always supreme.

We have suggested that the rule to be deduced from the decided cases, and from the nature of our constitutional government, is that any property which a state acquires and any activity which a state or political subdivision undertakes in order to furnish a public service to the inhabitants of the state or nation is constitutionally immune from federal taxation.

In analyzing the bases of state immunity we shall argue (1) that the states should be given the same freedom from tax burdens in enlarging their activities within the fields reserved to the states that the federal government has within the powers delegated to it; (2) that the general principles of state and federal immunity have been traditionally regarded as reciprocal and should continue to be so regarded; and (3) that no previous case has sustained a federal tax upon a public service rendered by a state or political subdivision.

(1) The states should be given the same freedom from tax burdens in enlarging their activities within the fields reserved to the states that the Federal Government has within the powers delegated to it.

It is not necessary to remind this Court how far the Federal Government has expanded its activities beyond what the founding fathers could have specifically foreseen in 1787. Government corporations are numbered by the score (see *Keifer & Keifer* v. *Reconstruction Finance Corp.*, 306 U. S. 381, 390n.), and departments themselves have engaged in businesses which might be described as comparable in character to private business. In fact this Court has observed of at least one Government corporation that its activities are "akin to those of private enterprises." *Reconstruction Finance Corp.* v. *Menihan Corp.*, 312 U. S. 81, 83.

All of these activities of the Federal Government have been declared governmental. The theory is that the Federal Government being one of delegated powers, any constitutional exercise of its powers must be governmental *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95, 102; *Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466, 478. Accordingly, any proper activity of the Federal Government is exempt from state or local taxation, unless Congress indicates a contrary intent. *City of Cleveland* v. *United States*, 323 U. S. 329, 333.

The governmental powers of the states, however, can be no less, within the fields reserved to the states, than the powers which the states have delegated to the Federal Government.

It has always been a function of government to supply to its citizens those services which for various reasons can be more advantageously rendered by the public than by private enterprise. As respects many of these services, the necessity of paying federal taxes would actually hamper the state in carrying on the activity, and might even pre-

vent the state from furnishing it to its citizens at a reasonable cost. In undertaking such projects as the distribution of water, the furnishing of low-cost housing, the building of bridges and the collection of garbage, and the operation of subways and other transit facilities, it is clear that states and cities are not actuated by commercial motives but by the same desire to fulfill the necessary functions of government which has led the Federal Government into new fields in recent years. There is no dependable historic basis for affirming that a specific activity has never been a part of state government, and no foresight is capable of affirming that a specific activity will never become an essential part of state government.

The same finding which the District Court made with respect to the State's sale of bottled waters, that it "had the characteristics of a business enterprise, and the waters referred to were sold in competition with private waters" (R. 27), could be made with reference to any number of federal activities with equal force.

This Court has not assumed to limit the expansion of activities by the states or to question the propriety of steps which do not infringe the due process clause or other provisions of the Federal Constitution. As was said in Mr. Justice Stone's opinion in *Puget Sound Power & Light Co.* v. *Seattle*, 291 U. S. 619, 624:

> "'In conducting the business by state authority the city is exercising a part of the sovereign power of the state which the Constitution has not curtailed. The decisions of this Court leave no doubt that a state may, in the public interest, constitutionally engage in a business commonly carried on by private enterprise, levy a tax to support it, *Green* v. *Frazier*, 253 U. S. 233; *Jones* v. *Portland*, 245 U. S. 217, and compete with private interests engaged in a like activity. *Standard Oil Co.* v. *Lincoln, supra; Madera Water Works* v. *Madera* 228 U. S. 454; *Helena Water Works Co.* v. *Helena*, 195 U. S. 383."

The broad extent of the states' powers is expressly recognized by the Tenth Amendment, which provides:

> "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people."

It should not be forgotten that it was the people of the States, as independent sovereignties, which ratified the Constitution and created the United States. WARREN, *The Supreme Court and Sovereign States* [1924] Apdx. B, pp. 105-112. As Mr. Justice William Johnson said, dissenting in *Bank of United States* v. *Planters' Bank of Georgia*, 9 Wheat. 904, 912, "in every possible form and shape, it is a sovereign state, or it is nothing".

The right of the states to enter new fields of activity under their reserved powers has contributed greatly to the progress of our country. As Mr. Justice Brandeis pointed out:

> "a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country". *New State Ice Co.* v. *Liebman*, 285 U. S. 262, 311.

The importance of tax immunity to give to the states the sovereign position to which they are entitled under the Constitution has been stated more than once.

> "The States are essential parts of the plan adopted by the Federal Constitution; and we accept as settled doctrine that the United States can lay no tax upon their governmental instrumentalities." (*Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393, 400.)

The contention advanced by the United States in this case, that any activity of a state which smacks of a business nature is outside the scope of governmental immunity, sounds in strange contrast to the views of the late

Governor Alfred E. Smith of New York about the conduct of government affairs. In his messages to the Legislature he often referred to the State's work in terms of business:

> "In the last analysis, we will have to deal with but very few strictly political problems. The activities of the great corporation known as the State of New York are almost entirely concerned with the strictly business side of government and the welfare or human side" (Annual Message Jan. 7, 1925—N. Y. Leg. Doc. No. 3, p. 4). (See also Annual Message Jan. 6, 1926—Public Papers of Governor Alfred E. Smith 1926, pp. 29-30.)

The fact that the Federal Government is exercising new powers in many fields should not be permitted to obscure the continued importance of the states themselves. Woodrow Wilson treated this problem with statesmanlike foresight in his lectures on "*Constitutional Government in the United States*" (1908). After describing the nationalizing process which was even then under way, he stated (p. 49):

> "But there are natural limits beyond which such a development cannot go, and our state governments are likely to become, not less, but more vital units in our system as the natural scope and limits of their powers are more clearly and permanently established".

The whole of Chapter VII of President Wilson's book, dealing with the relation between the states and the Federal Government, is of interest. We quote only a paragraph, dealing with the extent of the states' powers:

> "The presumption insisted upon by the courts in every argument with regard to the powers of the federal government is that it has no power not explicitly granted it by the federal Constitution or reasonably to be inferred as the natural or necessary accompaniment of the powers there indisputably conveyed to it;

but the presumption with regard to the powers of the States they have always held to be of exactly the opposite kind. It is that the States of course possess every power that government has ever anywhere exercised, except only those powers which their own constitutions or the Constitution of the United States explicitly or by plain inference withhold. They are the ordinary governments of the country; the federal government is its instrument only for particular purposes". (pp. 183-4).

The nature of the relation between the states and the Federal Government requires that legitimate state activities within the reserved powers of the states be left, so far as possible, free from any federal burdens or interference.

As Thomas Jefferson put it:

"The capital and leading object of the Constitution was to leave with the States all authorities which respected their own citizens only, and to transfer to the United States those which respected citizens of foreign or other States: to make us several as to ourselves, but one as to all others." (Letter to Mr. Justice Johnson, June 12, 1823, 15 The Writings of Thomas Jefferson [Lipscomb ed. 1905] 439.)

Hon. Franklin D. Roosevelt while he was Governor of New York said, in a radio address on States' Rights:

"Thus, already it was clear to the framers of our Constitution that the greatest possible liberty of self-government must be given to each state, and that any national administration attempting to make all laws for the whole nation, such as was wholly practical in Great Britain, would inevitably result at some future time in a dissolution of the Union itself." (Public Papers of Governor Franklin D. Roosevelt 1930, p. 710.)

The rapid expansion of social legislation by Congress in recent years should not be permitted to obscure the fact that the states have truly been the experimental laboratories throughout the history of our land. New

York created a State Insurance Fund for workmen's compensation in 1914 (L. 1913, c. 816; L. 1914, c. 41; Workmen's Compensation Law, Art. 6), before there was any federal provision either for workmen's compensation (the Longshoremen's and Harbor Workers Compensation Act was passed in 1927, 33 U. S. C. A. § 901, *et seq.*) or for insurance activity of any sort (*e. g.*, War Risk Insurance, War Damage Corporation, Federal Crop Insurance Corporation, etc.). Massachusetts (in 1874) was the first state to enact a ten-hour law for women (8 *Encyclopedia of the Social Sciences* 660). Nebraska insured bank deposits (see *Noble State Bank* v. *Haskell*, 219 U. S. 104, 575) long before there was a Federal Deposit Insurance Corporation. North Dakota undertook both farm marketing and public housing (*Green* v. *Frazier*, 253 U. S. 233) before there was either a Commodity Credit Corporation or a Federal Housing Administration. Oregon had minimum wage laws long before there was any Federal Fair Labor Standards Act (*Muller* v. *Oregon*, 208 U. S. 412). New York built the Erie Canal as a state enterprise in 1825, long before the Federal Government took over the Panama Canal from its private promoters or organized the Inland Waterways Corporation. And the list might be extended in similar fashion.

The scope of the federal income tax is so all-embracing that nothing would be left of state immunity if any activity, which in private hands would be subject to the income tax, was thereby taxable in the hands of the state as having been "withdrawn" from the federal taxing power.

No one can tell what future advances may be hampered if this court sanctions the burdening of any new state activity with federal taxes.

Many new activities would be seriously handicapped if they were required to pay federal taxes. A major reason for enlargement of state and municipal activities has been

the inability of private enterprise to furnish satisfactory services profitably. This is surely true in the transit field, and to some extent explains the taking over of highway construction as a governmental activity.* It is clear, moreover, that existing rules of immunity have not hampered the unprecedented tax programs of the war years.

This Court in very recent decisions has recognized the wisdom of not intruding upon the powers of the states. *Spector Motor Service, Inc.* v. *McLaughlin*, 323 U. S. 101; *Ford Motor Co.* v. *Department of Treasury*, 323 U. S. 459. The Court has declared that a state statute cannot be condemned as in conflict even with express national legislation unless the conflict is clearly shown. *Alabama State Federation of Labor* v. *McAdory*, 325 U. S. , 65 Sup. Ct. 1384, 1392 (June 11, 1945); compare *North Carolina* v. *United States*, 325 U. S. , 65 Sup. Ct. 1260, 1263 (June 11, 1945). By the same token the immunity inherent in any state activity should not be overruled as inconsistent with the Constitution unless there is some clear and compelling reason.

It is surely not in keeping with the respect this Court has expressed for the states, to take a niggardly or grudging attitude toward the extent of the states' governmental power to exercise the rights specifically reserved to them by the Constitution.

(2) The general rule is, and should continue to be, that the immunities of the States and of the Federal Government are reciprocal.

The decisions of this Court have established over a long period of years, that the immunity of the states from federal taxation is based on the same principles as the immu-

* Plank road corporations were chartered by the hundreds in the mid-nineteenth century, with power to improve highways and charge tolls, but the difficulties of private operation have forced the State to take over most highway activities (MAU, *The Development of Central and Western New York* [1944], 386-88).

nity of federal agencies from state taxation—in other words, that the two immunities are reciprocal.

The principle of federal supremacy within the fields delegated to the Congress may sometimes operate to enlarge the federal immunity or restrict that of the states, so that the latter may be held within narrower limits (*cf. Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466, 478, 489), but the basis of the two immunities is similar.

Chief Justice Marshall's words in *McCulloch* v. *Maryland*, 4 Wheat. 316, apply as well to a federal tax on a state agency as to a state tax on a federal agency.

> "If we measure the power of taxation residing in a state, by the extent of sovereignty which the people of a single state possess, and can confer on its government, we have an intelligible standard, applicable to every case to which the power may be applied. • • • We have a principle which is safe for the states, and safe for the Union. We are relieved, as we ought to be, from clashing sovereignty; from interfering powers; from a repugnancy between a right in one government to pull down, what there is an acknowledged right in another to build up; from the incompatibility of a right in one government to destroy, what there is a right in another to preserve. We are not driven to the perplexing inquiry, so unfit for the judicial department, what degree of taxation is the legitimate use, and what degree may amount to the abuse of the power" (pp. 429, 430).

It is true that Marshall, after holding the Bank to be constitutional, invoked the supremacy clause of the Federal Constitution as one of his arguments to protect it, but the decision does not rest on that alone. The supremacy clause (Art. VI, § 2) applies to federal laws within the powers delegated to Congress, but state laws are equally binding within the fields reserved to the states. *Tompkins* v. *Erie Railroad Co.*, 304 U. S. 64; and *Cf.* 4 Wheat. at 410.

The fact that the initial opinion of the great Chief Justice in the *McCulloch* case discussed possible differences between the states and the federal goverment lends added weight to the statements in subsequent cases that the immunities of the two governments are founded on the same basis. It is not to be supposed that the judges who applied and repeated the doctrine of reciprocal immunity through the years were ignorant of what the opinion in the *McCulloch* case said. The *McCulloch* case was expressly referred to in one of the earliest cases to state the rule of reciprocal immunity, that of *New York ex rel. Bank of Commerce* v. *Commissioners of Taxes*, 2 Black 620, 635, where the Court stated:

> "Each is sovereign and independent in its sphere of action, and exempt from the interference or control of the other, either in the means employed or functions exercised * * *".

No other statement would have been consistent with the view expressed by the framers of the Constitution, that the taxing powers of the state and federal governments were to be concurrent. *The Federalist* (Ford ed. 1898) Nos. 30-36, esp. pp. 199, 212.

Nor may the *McCulloch* case be explained away as based on an outworn belief that the power to tax is the power to destroy. Chief Justice Marshall was expressing in vivid fashion the possible effect of a tax; but the principles of immunity, necessary to accommodate the respective interests of the state and federal governments, demand protection from taxes which interfere with sovereign operations as well as those which would utterly destroy them.

The rule of reciprocal immunity was clearly expressed in *Collector* v. *Day*, 11 Wall. 113, where Mr. Justice Nelson stated:

> "the States within the limits of their powers not granted, or, in the language of the tenth amendment, 'reserved,' are as independent of the general govern-

ment as that government within its sphere is independent of the states" (p. 124).

> "in this respect, that is, in respect to the reserved powers, the State is as sovereign and independent as the general government. And if the means and instrumentalities employed by that government to carry into operation the powers granted to it are, necessarily, and, for the sake of self-preservation, exempt from taxation by the States, why are not those of the States depending upon their reserved powers, for like reasons, equally exempt from Federal taxation? Their unimpaired existence in the one case is as essential as in the other" (p. 127).

This rule was repeated in *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 584:

> "As the States cannot tax the powers, the operations, or the property of the United States, nor the means which they employ to carry their powers into execution, so it has been held that the United States have no power under the Constitution to tax either the instrumentalities or the property of a State."

The reciprocal nature of the immunity was acknowledged again by Mr. Justice Shiras in *Plummer* v. *Coler*, 178 U. S. 115, which held that a state inheritance tax might include United States bonds as part of the estate. He stated (p. 117):

> "It is not open to question that a State cannot, in the exercise of the power of taxation, tax obligations of the United States. *Weston* v. *Charleston*, 2 Pet. 449; *Bank of Commerce* v. *New York City*, 2 Black, 620; *Home Insurance Co.* v. *New York*, 134 U. S. 594, 598.
>
> So, likewise, it is settled law that bonds issued by a State, or under its authority by its public municipal bodies, are not taxable by the United States. *Mercantile Bank* v. *New York*, 121 U. S. 138, *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 583.
>
> The reasoning upon which these two lines of decision proceed is the same."

Similarly, Chief Justice Fuller, in *Ambrosini* v. *United States*, 187 U. S. 1, construing a statute exempting state bonds from stamp taxes, stated (p. 7):

> "The general principle is that as the means and instrumentalities employed by the General Government to carry into operation the powers granted to it are exempt from taxation by the States, so are those of the States exempt from taxation by the General Government."

Again in *Farmers and Mechanics Savings Bank* v. *Minnesota*, 232 U. S. 516, Mr. Justice Pitney, in forbidding a state to tax bonds issued by municipalities in Indian Territory, stated, after quoting the rule that a tax on government bonds is a tax on the operation of government, that (pp. 526-527):

> "It is on this ground that United States bonds have always been held exempt from taxation under authority of the States. By like reasoning it has come to be recognized that bonds issued by the States are not taxable by the Federal Government."

In *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 521, the Court said:

> "We pass to the more difficult question whether Congress had the constitutional power to impose the tax in question, and this must be answered by ascertaining whether its effect is such as to bring it within the purview of those decisions holding that the very nature of our constitutional system of dual sovereign governments is such as impliedly to prohibit the federal government from taxing the instrumentalities of a state government, and *in a similar manner* to limit the power of the states to tax the instrumentalities of the federal government."

Mr. Justice Stone in *Educational Films Corp.* v. *Ward*, 282 U. S. 379, 389, stated that "the instrumentalities of either government, or the income derived from them, may not be made the direct object of taxation by the other."

The reciprocal nature of the immunities was reiterated in *Trinityfarm Construction Co.* v. *Grosjean*, 291 U. S. 466, where a state excise tax on gasoline purchased by a federal contractor was held to have only a remote effect upon the federal government. Speaking of the principle that a state could not tax a federal instrumentality the Court said (p. 471):

> "That principle, while not expressly stated in the Constitution, necessarily arises out of our dual government. It has often been given effect. And reciprocally it safeguards every State against federal tax on its governmental agencies or operations."

Reciprocity seems also to be assumed by Mr. Justice Stone in *United States* v. *California*, 297 U. S. 175, 184, where he states that:

> "Its nature requires that it be so construed as to allow to each government reasonable scope for its taxing power, see *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 522-524, which would be unduly curtailed if *either* by extending its activities could withdraw from the taxing power of the other subjects of taxation traditionally within it."

Cf. Cardozo, J., dissenting, in *Ashton* v. *Cameron County Water Improvement District*, 298 U. S. 513, 540.

Both opinions in the *Brush* case recognized the rule of reciprocal immunity. The majority opinion stated:

> "The unimpaired existence of both governments is equally essential. It is to that high end that this court has recognized the rule, which rests upon necessary implication, that neither may tax the governmental means and instrumentalities of the other" (300 U. S. at 364).

The dissenting opinion of Mr. Justice Roberts, with whom Mr. Justice Brandeis joined, stated (300 U. S. at 375):

> "It seems to me that the reciprocal rights and immunities of the national and a state government may

be safeguarded by the observance of two limitations upon their respective powers of taxation. These are that the exactions of the one must not discriminate against the means and instrumentalities of the other and must not directly burden the operations of that other."

See also *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, 575;

New York ex rel. Cohn v. *Graves*, 300 U. S. 308, 315-16;

Helvering v. *Therrell*, 303 U. S. 218, 223;

Hon. Stanley Reed, *The State Today*, 15 Tenn. L. Rev. 52, 62 (1937);

COOLEY, *Constitutional Limitations* (1868) p. 483.

So, developments in the law of federal and state tax immunity have run hand in hand.

Thus, *Dobbins* v. *Commissioner*, 16 Pet. 434, exempting the salaries of federal officers from state taxation, was followed by *Collector* v. *Day*, 11 Wall. 113, exempting the salaries of state officers from federal taxation, and "for like reasons." See *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, 577.

Conversely, *United States* v. *Perkins*, 163 U. S. 625, permitting a state tax upon a bequest to the Federal Government, as an excise upon the power to transmit by will, was followed by *Snyder* v. *Bettman*, 190 U. S. 249, upholding a federal tax on legacies to states or municipalities.

When this Court approved a federal tax on the income of a lessee of state oil land (*Helvering* v. *Mountain Producers Corp.*, 303 U. S. 376), it expressly overruled both the case which had previously forbidden such a federal tax (*Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393) and also the decision which had forbidden a state tax upon the in-

come of a lessee of restricted Indian lands (*Gillespie* v. *Oklahoma*, 257 U. S. 501).

When the Court determined that a tax on salaries was not a direct burden on the government paying the salaries, its decision permitting a federal tax on salaries of state officers (*Helvering* v. *Gerhardt*, 304 U. S. 405) was quickly followed by a decision permitting a state tax on the salaries of federal officers. *Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466.

The statement which the Court has recently made, that any constitutional exercise of federal powers must be governmental, because the Federal Government has only delegated powers (*Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95, 102), must be supported by some unexpressed minor premise, either that the states (or their people) which delegated the power to the Federal Government possessed only governmental powers, or that their intention was to delegate only governmental powers. Under the first alternative, every activity of a state must be treated as governmental; under the second, any activity in which the Federal Government participates must also be governmental when undertaken by a state or municipality.

The argument that the states have less need of immunity than the Federal Government, because they are represented in Congress (see *Helvering* v. *Gerhardt*, 304 U. S. at 416), cannot be pressed too far. Such an answer is never in itself a satisfactory response to a constitutional question. Wisconsin was represented in the Congress when it passed the Home Owners' Loan Act of 1933, yet Mr. Justice Cardozo for a unanimous Court held that the Congress did not have power under the Federal Constitution to authorize a state-chartered savings and loan association to convert into a federal association without the consent of the state. *Hopkins Federal Savings and Loan Association* v. *Cleary*, 296 U. S. 315. The truth is that so

many complicated elements influence the final passage of a Congressional act that it would be a mistake to regard it in every case as representing the final word on the rights of the states under the Constitution. Moreover, long-range planning, essential to large public projects, would be subject to new difficulties if the immunity of the project were to depend upon the will of fluctuating majorities in Congress rather than upon the relative security of constitutional doctrine. Approaching the point from another angle, it has been suggested that the power of Congress to protect a federal enterprise from state taxation is a power of self-defense that no state possesses through its own legislature. T. R. Powell, *The Waning of Intergovernmental Tax Immunities,* 58 Harv. L. Rev. 633, 653-54, 649.

Incongruous and unhappy results may follow from failure to adhere to the principle of reciprocity.

It may be suggested that the principle of reciprocal immunity is unimportant here because the Federal Government does not sell *bottled* mineral water (R. 19). It is within the realm of possibility, however, that the Federal Government may at some time bottle and sell water from the geysers at Yellowstone Park or from the springs which it owns at Hot Springs, Ark. It is engaged in many other activities in the National Parks which are of a commercial nature. See Report of the Secretary of the Interior for the fiscal year ending June 30, 1941, describing the activities of National Park Concessions, Inc., a non-profit corporation organized to operate concession facilities—page 279; same for 1942, page 163; same for 1943, page 217. A holding that the sale of water from Saratoga Springs is not a governmental activity would require a parallel holding, if the Department of Interior should ever seek to sell mineral waters, that it was not within the governmental powers delegated to the United States.

To take another example, the Federal Government is developing power from the Tennessee River, and this Court has stated that in so doing it is "performing a governmental function." *Graves* v. *Texas Company*, 298 U. S. 393, 395.* One of the early T. V. A. contracts was with the cities of Tupelo, Miss. and Athens, Ala., which owned municipal distribution systems. PRITCHETT, *The Tennessee Valley Authority, A Study in Public Administration* (1943) 67. The distribution of electricity must be as much a governmental function as the production of that same electricity, yet the position urged by the United States in this case might require that the two be treated differently.

The housing field likewise emphasizes the need of applying reciprocal immunity. The same public needs which have led the Federal Government to assist in providing housing for low-income groups have impelled the states to erect housing developments at public expense (N. Y. Const., Art. XVIII; N. Y. Public Housing Law). The provision of housing is not a traditional governmental activity in the narrow sense, but it responds to a public need and to local conditions, which the states should have freedom of action to remedy. Yet a denial

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* The decision of the three-judge district court listed the Tennessee Valley Authority as one of the federal agencies to which the Texas Company was selling gasoline. *Texas Co.* v. *Carmichael*, 13 F. Supp. 242, 248n. Circuit Judge Hutcheson, in his dissenting opinion in that court, pointed out that:

> "If the establishment of departments of liquor control, as in the South Carolina and Ohio cases, and the operation of a railroad, as in Helvering v. Powers, are not the exercise by the state of ordinary and usual governmental functions within the principle of exemption from federal taxation, it would seem probable that some of the agencies which plaintiff's gasoline will activate will not be within the principle of exemption from state tax" (13 F. Supp. at 249).

of the doctrine of reciprocal immunity might hamper state housing by permitting the imposition of an income tax on the revenues of a housing authority if they exceed the normal depreciation of the buildings, or even on the interest paid to holders of housing authority bonds.

If this Court were to hold that state activities may be subject to any non-discriminatory tax which the Federal Government undertakes to levy, the result would be to put the States at a serious disadvantage in meeting the needs of their citizens.

(3) No previous case has sustained a federal tax upon a public service rendered by a state or political subdivision.

The rule of tax immunity commences with the sense that there is something unseemly and constitutionally objectionable in one government imposing taxation on another. This objection extends to any activity by which a government is serving a genuine public purpose.

In determining the extent of state activities which may be accorded tax immunity, the Court should apply the principle it has announced in other connections, that "there is wide discretion on the part of the legislature in determining what is and what is not necessary—a discretion which courts ordinarily will not interfere with" *Manigault* v. *Springs*, 199 U. S. 480-81, quoted in *East New York Savings Bank* v. *Hahn* 325 U. S. . (Nov. 5, 1945).

This Court has not, we are sure, meant to import the artificial distinctions of tort law into constitutional law by referring to "governmental" functions as the limit of state immunity. The tort cases were referred to by way of analogy only in the *South Carolina* case, 199 U. S. at 461, and the confusion which existed in the field of tort law was one of the grounds for the dissent in that case (p. 471). The intervening years have only added to the

confusion.* Recently Mr. Justice Black has pointed out the latitude for dispute which exists in defining "essential governmental functions." *Helvering* v. *Gerhardt*, 304 U. S. at 426.

Analysis of the practical effect of this Court's prior decisions concerning immunity of state activities supports as a minimum rule of state immunity, that any genuine public service rendered by states or municipalities is essentially "governmental" and is entitled to immunity from federal taxation. That immunity may attach, although the service was once largely within the field of private enterprise, and still is covered in part by private agencies, is shown by *Brush* v. *Commissioner*, 300 U. S. 352, 371, where this Court held that the supplying of water should be recognized as a governmental function.

It is noteworthy also that the opinion in the *Brush* case refused to be controlled by local law as to classification of activities for tort liability (300 U. S. at 363-65). A comparable instance where this Court refused to transfer common law distinctions (as to the difference between "employee" and "independent contractor"), into another field is *National Labor Relations Board* v. *Hearst Publications, Inc.*, 322 U. S. 111 (see particularly pp. 120-22 and 126-29). In the field of state immunity from direct taxation, there is ample justification for this Court's adopting a standard of what is "governmental" which would include all public services and exclude only commercial enterprises which were embarked upon for profit alone.

The fact that the issue related to a claimed exemption from personal income tax must be borne in mind in considering *Helvering* v. *Powers*, 293 U. S. 214, which is cited (United States brief, p. 13) for the proposition that the

* New York has recently cut the Gordian knot by imposing liability for all acts not only of the state, but also of municipal corporations, whether previously considered proprietary or governmental. Bernardine v. City of New York, 294 N. Y. 361.

operation of a street railway lies outside the scope of constitutional state immunity. The statements in that case that operation of the street railway system directly by the State Government would not bring immunity from federal taxing power were not necessary for the decision of the case, for there were substantial indications that the officers whose salaries were there sought to be exempted were not truly state officers. Although appointed by the Governor to manage the affairs of the Boston Elevated Railway Company, they received their compensation from the company (p. 220) and the property of the company remained in private ownership (p. 223). A holding that such state-appointed managers of a private company were governmental instrumentalities would scarcely have been consistent with prior rulings that receivers of private corporations, appointed by federal courts, were not governmental instrumentalities (*Michigan* v. *Michigan Trust Co.*, 286 U. S. 334; *Gillis* v. *California*, 293 U. S. 62). Moreover, the *Powers* case was decided before this Court had held in *New York ex rel. Rogers* v. *Graves*, 299 U. S. 401, that the operation of a railroad by the Federal Government was an activity entitled to immunity from state taxation. The *Powers* case was apparently not cited in the *Rogers* case, but it may be doubted whether the same reasoning would have been stated thereafter.

There are three cases cited in the United States brief (pp. 12-13) in which the States have been denied immunity from taxes imposed directly upon state activities.

South Carolina v. *United States*, 199 U. S. 437;
Ohio v. *Helvering*, 292 U. S. 360;
Allen v. *Regents*, 304 U. S. 439.

All these cases are consistent with recognition of immunity in the present case, provided that their facts be viewed as this Court viewed them when it decided them, and not as it might now view them. None of them involved the furnishing of a public service necessary to the citizens of the State, and in each of them there were ex-

ceptional circumstances which seemed to outweigh the principle of state immunity.

In *South Carolina* v. *United States*, 199 U. S. 437, the majority opinion of this Court said it was confronted with a threat to the "whole body of internal revenue tax" (p. 454). It could perceive no relevant difference between state sale of liquor through dispensaries, and sale, "in like manner, of tobacco, oleomargarine, and all other objects of internal revenue tax." The extent of the Court's fears, and the bearing on the ultimate decision of its antipathy to public ownership, are exemplified in the following quotation from Mr. Justice Brewer's opinion (p. 454):

> "If one State finds it thus profitable other States may follow, and the whole body of internal revenue tax be thus stricken down.
>
> More than this. There is a large and growing movement in the country in favor of the acquisition and management by the public of what are termed 'public utilities', including not merely therein the supply of gas and water, but also the entire railroad system. Would the State by taking into possession these public utilities lose its republican form of government?"

The majority's concern over the threat to private business is also indicated by its quotation at page 457. It may be that persons today will consider those several alarms excessive, as did the three dissenting justices in that case (pp. 470-472), but for purposes of understanding the decision the statement of the case by the majority is the true guide, and the majority saw abundant reason why the principle of state immunity was outweighed.*

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* Acting United States Attorney-General John W. Davis distinguished the *South Carolina* case in an opinion which ruled that the Pennsylvania Workmen's Compensation Fund was exercising an "essential governmental function", suggesting that the earlier case was based on "some peculiar circumstances connected with it, as e.g., the direct entrance of the State into the liquor business for a profit, and the lack of clear connections between such a business connection and any real regulation of the liquor traffic, so that the court was justified in describing it as a 'private business'". 31 Ops. Atty. Gen. 308, 317 (1919).

The *South Carolina* case can best be understood in the light of the sources of federal revenue at the time. In 1905, when the case was decided, over one-fourth of the entire annual income of the Federal Government was derived from taxes on spirits and fermented liquors.* It is understandable that the Court feared what might be the effect on the Federal Government if immunity were recognized and other states followed South Carolina's example. Clearly no such results would ensue if New York's sales of mineral waters were held to be free of a federal tax which amounts to only $4,473.50 (R. 22).

Ohio v. *Helvering*, 292 U. S. 360, was decided upon an application to file an original suit in this Court, opposed by the United States upon the ground that it did not satisfy the jurisdictional requirements and was an injunction against collection of a Federal tax, forbidden by Revised Statutes § 3224. Apparently there was no argument and the briefs were of the summary nature suitable to a preliminary motion. Although the State attempted to distinguish the considerations which were prompting it to enter the liquor dispensary business in 1933 from those which moved South Carolina in 1895 (pp. 364-365), the opinion by Mr. Justice Sutherland referred to the South Carolina case as one "in no substantial respect distin-

---

* The Annual Report of the Secretary of the Treasury on the State of Finances for the Fiscal Year ended June 30, 1905 shows the following figures:

Total receipts from all sources	$697,101,269.95 (p. 1)
Total internal revenue	234,187,976.37 (p. 467)
Total revenue on spirits	135,958,513.12 (p. 466)
Total revenue on fermented liquors	50,360,553.18 (p. 466)

By contrast the total tax receipts from all mineral or table waters during the fiscal year 1933 amounted to only $144,947.12 (See Revenue Revision, 1934, being Hearings before the Committee on Ways and Means of the House of Representatives, 73d Congress, 2d Session, p. 883), out of total revenue receipts of $2,037,701,617.66 (Annual Report of Secretary of the Treasury for 1933, p. 329).

guishable from the present one" (p. 368). The attempted distinction as to the sale of liquor, and particularly in Ohio in 1933, was dismissed as "altogether fanciful" (p. 369).

In *Allen* v. *Regents*, 304 U. S. 439, although it was assumed that the holding of athletic contests is an integral part of the program of public education conducted by Georgia (p. 449), the statistics recited at page 450 suggested doubt as to the closeness of the relationship,* and the case was viewed as one where a state had deliberately embarked upon a business for profit, to be judged by the liquor dispensary precedents (p. 451). As its final argument, the opinion referred to the "destruction of the federal power to tax which might result from a contrary decision," and relied upon all the alarms of the *South Carolina* case (p. 453).

The facts in the *Allen* case also weaken its validity as a holding that a tax may be imposed directly upon the State Government. In a large degree the burden of the tax fell on the football spectators. The Commissioner of Internal Revenue had ruled that state universities must collect the tax on admissions "because the burden of the tax falls, not on the state, but on the persons paying the admission charges" (*Allen* Record, p. 8). The Regents had accordingly paid over the tax in earlier years to the Treasury, and when a refund was denied abandoned any claim for that period, "believing that the basis of the Commissioner's refusal to refund was sound" (304 U. S.

* The same doubt is expressed in a report of the Carnegie Foundation for the Advancement of Teaching, quoted in a note on the District Court's decision in the *Allen* case. "The football contest * * * is not a student's game. * * * It is a highly organized commercial enterprise." (23 Va. L. Rev. 570, 577; Bulletin Number Twenty-three, Carnegie Foundation, American College Athletics, 1929, p. viii.)

at 446). They then resorted to the "expedient" (p. 446) of stating the amount as a tax on the ticket, but reciting that the liability to such tax was disputed, and that it would be retained as part of the admission fee unless it was finally determined that the University was subject to the tax (304 U. S. at 443). The only tickets on which tax was required to be paid were those sold to the general public, for students were admitted by virtue of an annual athletic fee which was free from tax (304 U. S. at 445n.). Although the opinion proceeded on the basis "that the tax is imposed directly on the state activity and directly burdens that activity" (304 U. S. at 449-50), this hypothesis must be taken at somewhat less than face value, for the reasoning under which the Court had upheld jurisdiction of the suit as one not forbidden by R. S. § 3224 (forbidding injunctions against the collection of a tax) was that "here the assessment is not of a tax payable by respondent but of a penalty for failure to collect it from another" (p. 449).

The policy of developing Saratoga Springs as a state health resort was adopted many years before the tax on bottled water was imposed and the tax was repealed after being in force for less than two years (Revenue Act of 1934, § 601-48 Stat. 762) (R. 13). There had been only one other short period, during World War I, when any tax was imposed on bottled waters (§ 313-c of 1917 Revenue Act—40 Stat. 312, repealed February 24, 1919—40 Stat. 1149).

The facts of the *South Carolina* case suggest that the extent of federal revenue dependent upon the particular field before the state enters it may be a factor in determining whether the state's normal tax immunity must yield. The Court explained the *South Carolina* case in *Murray* v. *Wilson Distilling Co.*, 213 U. S. 151 (where it held that South Carolina was entitled to sovereign im-

munity under the Eleventh Amendment, as against suit for liquor dispensary transactions) and stated that the issue in that case had been the State's power "to destroy a pre-existing right of taxation possessed by the government of the United States" (p. 173). This Court in *United States* v. *California* mentioned both the matter of "the activities in which the States have traditionally engaged" and the question whether either government "could withdraw from the taxing power of the other subjects of taxation traditionally within it" (297 U. S. 184-185); but it was not called upon to determine which was more important, the traditional character of the state activity or the traditional exercise of the federal taxing power.

We submit that it is more compatible with the reason of the rule to mark the limits of immunity by reference to previous federal taxes than by reference to previous state activity.

If every new state activity which might conceivably be made the subject of federal taxation were to be denied exemption, there would be little left of the principle of state immunity, for the field of federal excise taxation is almost limitless.

It is not consistent with the progressive attitude of this Court toward new state activities to say that they are undertaken at the risk of future federal taxation. Even if the Court still fears that the states, by undertaking activities which have been customarily the subject of special federal taxes, may create a sufficiently serious threat to the federal revenues to justify an exception to the general rule of immunity, as was made in the *South Carolina* case, the danger to the federal revenue from a state entering activities which are not at the time subject to federal tax is not sufficient to deny immunity.

These considerations only emphasize the fact that the sale of bottled water at Saratoga Springs is more like the supplying of water for a fee, held governmental in the *Brush* case, than the creation of a state monopoly for liquor sales, involved in the *South Carolina* case.

Giving due weight to the long line of cases which have declared immunity from a non-discriminatory tax imposed directly upon either State or Federal Government, to the doctrine that a state's disposal of natural resources and particularly of water is a governmental function, to the generally reciprocal character of state and federal tax immunities, to the policy of encouraging experimentation within the insulated cells of the states, and to the lack of any serious impairment here of the federal revenue, there appears to be no substantial ground for denying immunity to the State of New York in the present case.

Conclusion

Viewing this case as an isolated instance of state activity, we submit that the sale of bottled water at Saratoga Springs is entitled to immunity from federal taxation as a governmental activity in the interest of public health, and as an exercise of the State's undoubted right to control and dispose of the natural resources within its boundaries.

If the case be viewed as an occasion for reëxamining and restating the doctrine of intergovernmental tax immunity, we submit that this Court should abide by its oft-repeated declarations that the States are immune from taxes levied directly upon them even though non-dis-

criminatory, and that taxation is permitted, if at all, only where exceptional circumstances, not here present, give controlling weight to some competing principle.

The judgment appealed from should be reversed and the complaint dismissed.

Dated, Albany, N. Y., November 23, 1945.

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We join in the foregoing brief.

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JOHN A. SLADE,
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Appendix A.

Federal Taxing Statute

The tax here involved was imposed under the Federal Revenue Act of 1932. Section 615 (a) (5) thereof reads as follows:

> "There is hereby imposed * * * (5) upon all natural or artificial mineral waters or table waters, whether carbonated or not, and all imitations thereof, sold by the producer, bottler or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of 2 cents per gallon." (47 Stat. 265).

New York Statute

The statute regulating the Saratoga Springs Reservation at the time the Federal tax was imposed was Chapter 866 of the Laws of 1930, which contains the following provisions:

> "Section 1. **Commission established; organization; purpose.** A temporary state commission, to be known as the Saratoga Springs commission, is hereby created * * * for the purpose of ultimately developing the Saratoga Springs reservation as a state health resort and spa for use by the public for balneological, therapeutic and other similar healthful purposes. The development of such reservation for public health purposes is hereby declared a policy of the state * * *.
>
> "§ 5. **General powers and duties of commission.** The commission shall have the power and it shall be its duty, subject to the provisions of this act, to conserve, maintain, control and develop each and every part of the reservation property. * * * The commission may prescribe the terms upon which any excess of mineral water and gas not used on said reservation or used under such leases or concessions, shall be sold or distributed, and shall prescribe the names, labels and advertisements to be affixed to the

bottles or other vessels containing such waters, gases or other products, and may itself sell or dispose of the same. * * * The commission may make or cause to be made scientific studies and experiments concerning kinds of illnesses and diseases which lend themselves to the treatment of the mineral waters, products and facilities of the reservation, and shall exercise exclusive control and supervision over the manner and method of the use of the products and facilities of the reservation." * * *

"§ 10. **Projects to be planned and completed by commission.**

* * * *

The commission is hereby authorized and empowered to maintain and conduct the bath houses now on said reservation and such other bath houses as the commission may from time to time cause to be erected; to maintain and conduct the drink-halls on said reservation and such others as may be built under the supervision of the commission; and also to maintain and conduct the bottling plant now on said reservation and is further authorized and empowered to enlarge or rebuild the same or construct a new and more adequate one as, in its discretion, will be most advantageous." * * *

"§ 11. **Capital fund of commission.** * * * The commission shall deposit at least once in each week in the depository or depositories designated by the [state] comptroller all moneys received by it for all purposes."

Earlier statutes affecting the Reservation are referred to in the Stipulation of Fact (R. 31-32).

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Supreme Court of the United States

OCTOBER TERM, 1945

No. 5

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

UNITED STATES OF AMERICA.

SUPPLEMENTAL BRIEF FOR THE STATE OF NEW YORK

NATHANIEL L. GOLDSTEIN,
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We are conscious of the limited potentialities of an additional brief submitted at this stage of the case, and shall endeavor to avoid repetition. The briefs already submitted for the States answer substantially all that has been said by the United States.*

What we wish mainly to emphasize in this brief is that adoption of the principles urged by the United States would lead this Court into a new and uncharted sea of uncertainty. The United States would have this Court use the present case, in effect, as a vehicle for a declaratory judgment as to the validity of various unspecified future

* We add here as a matter of information the citation of *Arlington Hotel Co.* v. *Fant*, 278 U. S. 439, which we mentioned during the argument, as illustrating a comparable federal activity.

taxes upon state activities, or of the repeal of exemptions enacted in the belief that they were required by the Constitution. It seems to be conceded that the nature of our federal system imposes some limits upon the taxing power of the Federal Government, to which the word "nondiscriminatory" does not provide an all-sufficient answer. If this Court departs from the previously accepted standards it will be inviting a welter of new litigation to redefine the boundaries. The suggestion at the argument that Congress might tax public power activities of the states while continuing to sponsor federal power projects illustrates just one of the inevitable problems.

New York's suggestion that the case should be decided by comparison with the *Brush* and *South Carolina* cases (Supp. br., p. 50) involves no such complication; nor does the test of whether the State is serving the public health, safety and welfare, a test which was not only pronounced in the *Brush* case (300 U. S. at 371), but has been applied in other fields of state action (cf. *Treigle* v. *Acme Homestead Ass'n*, 297 U. S. 189; *Veix* v. *Sixth Ward Building & Loan Ass'n*, 310 U. S. 32, 41).

The United States argues (Supp. br., pp. 9-10) that because other types of tax or regulation may impinge upon state activities, the States have no need of immunity from taxes laid directly upon them. It might be urged with equal force that sales taxes and use taxes impose such burdens upon the Federal Government that direct taxation of federal activities should also be permitted. But the Federal Government has not only secured constitutional immunity from direct taxation; it has even found it necessary to devise new procedures to escape the burdens of indirect taxation (cf. Note, *Tax Avoidance by the Federal Government*, 19 St. John's L. Rev. 117). This argument should have no greater validity against the States than against the United States.

To characterize state immunity as a "subsidy" (U. S. Supp. br., p. 17) implies a predetermination of the issue. Under the teaching of the Court's prior decisions, state immunity is merely the price of maintaining our federal system of local self-government through the forty-eight states. The price has not proved unduly burdensome in the past, and there is no evidence that it is becoming so. As for the suggestion that a tax might be invalid if applied to private property but not to state property, one of the cases cited in our brief on reargument points out the justification for classifying private corporations differently from activities conducted by a municipal corporation (see *Puget Sound Power & Light Co.* v. *Seattle*, 291 U. S. 619, 624)—a classification which has been repeatedly made in the past.

The United States fears lest this Court strike down the power of Congress for the unforeseeable future, but the *South Carolina* case shows that this Court can always retain some measure of control. (Thus answering Mr. Justice Bradley's fears in *Collector* v. *Day*, 11 Wall. at 129.) On the other hand, the type of judicial self-abnegation which the United States proposes will leave the States at the mercy of Congress for the unpredictable future, without their being able to look to this Court as the ultimate and impartial umpire between state and nation.

This Court's judicial competence is not restricted to common law issues or statutory construction. One of the important phases of its exercise is the resolving of problems of how far the States may exercise their reserved powers under particular factual settings without infringing upon the powers committed to Congress (cf. *California* v. *Thompson*, 313 U. S. 109; *Parker* v. *Brown*, 317 U. S. 341, 359-68). That is essentially the type of issue which is involved here.

The suggestion made at the argument, that although the the present case involves only a small amount, nevertheless "many little things make much", and that the case should be viewed as if there had already been the greatest conceivable multiplication of state transactions; is equivalent to an argument that since the last straw breaks the camel's back, not even one straw should be allowed. Mr. Justice Holmes pointed out the fallacy in this assumption when he stated in *Panhandle Oil Company* v. *Mississippi*, 277 U. S. 218, 223, that "In those days it was not recognized as it is today that most of the distinctions of the law are distinctions of degree. If the States had any power it was assumed that they had all power, and that the necessary alternative was to deny it altogether."

The attorney for the United States argued that the claim of state immunity "rests really on the apprehension that unless immunity is granted, somehow the existence of the state is threatened." This is a curious reversal of reasoning. The apprehension in the *South Carolina* case was lest immunity be carried so far that the Federal Government be destroyed. The case is not one of a state coming as a suppliant and craving the boon of immunity, but rather presents a problem of whether the Federal Government has any right to tax another government which is of equal importance in the light of the Constitution—and to what extent, if any taxation must be permitted in order to preserve the Federal Government. That the United States is arguing for a radical change in the rules of immunity was made apparent when counsel stated the problem as being whether the time has not come "to abandon" the immunity.

The announcement, in the setting of this rather narrow litigation, of a new principle of intergovernmental relations not essential to a decision of the case, would unbalance the scales. This is not a time when the United

States needs protection against the States. It is rather a time when local self-government should be encouraged, in order that there may be no unnecessary obstacle to free experimentation in meeting the diverse problems of our era.

The judgment under review should be reversed and the complaint dismissed.

Dated, Albany, N. Y., December 11, 1945.

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No. 996 83

In the Supreme Court of the United States

OCTOBER TERM, 1943

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The opinion of the District Court (R. 32–39) is reported in 48 F. Supp. 15. The opinion of the Circuit Court of Appeals (R. 50–54) is reported in 140 F. 2d 608.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 23, 1944 (R. 54). The petition for a writ of certiorari was filed May 12, 1944. The jurisdiction of this Court is invoked

under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the State of New York and its agencies are entitled to immunity from the Federal excise taxes imposed by Section 615 (a) (5) of the Revenue Act of 1932 in respect of certain mineral and table waters bottled and sold by the agencies.

STATUTE AND CONSTITUTIONAL PROVISIONS INVOLVED

Constitution of the United States:

ARTICLE I.

SECTION 8. The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States;

* * * * * *

TENTH AMENDMENT

The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.

Revenue Act of 1932, c. 209, 47 Stat. 169:

TITLE IV—MANUFACTURERS' EXCISE TAXES

* * * * * *

SEC. 615. TAX ON SOFT DRINKS.

(a) There is hereby imposed—

* * * * * *

(5) Upon all natural or artificial mineral waters or table waters, whether carbonated or not, and all imitations thereof, sold by the producer, bottler, or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of 2 cents per gallon.

* * * * * *

STATEMENT

This is a suit by the United States to collect taxes, interest and penalties assessed on the bottling for sale and sale in closed containers of natural mineral and table waters at a price in excess of 12½ cents per gallon by the Saratoga Springs Commission and the Saratoga Springs Authority during the period June 21, 1932, to May 10, 1934, inclusive (R. 15–16).

The Saratoga Springs Commission (hereinafter referred to as the Commission) is a public commission of the State of New York (hereinafter referred to as the State), which was created in 1930 as a temporary commission for a term of seven years and continued in 1937 as a permanent commission (R. 16). The Saratoga Springs Authority (hereinafter referred to as the Authority) is a public benefit corporation of the State created in 1933 to take over the management of a State Reservation at Saratoga Springs (hereinafter referred to as the Reservation) by lease from the Commission (R. 16). The Authority was established in order to obtain

a loan from the Reconstruction Finance Corporation to aid in the further development of the Reservation for public health purposes in accordance with the declared policy of the State (R. 16).

During the period June 21, 1932, to May 10, 1934, inclusive, the Commission and Authority bottled for sale and sold in closed containers certain natural mineral and spring waters at a price in excess of 12½ cents per gallon to various vendees within and without the State (R. 17). Returns disclosing the amount of tax payable, if due, on the sales made during this period were filed under protest with the Federal Collector of Internal Revenue at Albany, New York (R. 17). The returns were filed by the Commission for the period June 1932 to September 1933, inclusive, and by the Authority for the period, October 1933 to May 1934, inclusive (R. 17). A statement was attached to each return that no tax was due upon the ground that the sale of the waters by the State was the exercise of a governmental function (R. 17). The taxes in the amounts disclosed by the returns, together with interest and penalties, were assessed by the Commissioner of Internal Revenue and notices and demands for payment were issued upon the proper parties (R. 17), but no part thereof has been paid (R. 19).

The waters, the bottling and sale of which gave rise to the instant controversy, came from min-

eral springs on the Reservation in the vicinity of Saratoga Springs, New York (R. 19). The waters are characterized by a supersaturation of carbon dioxide gas, and contains, in various quantities and combinations, minerals in solution, the most common of which are salt, soda, calcium, magnesium, and iron in the form of chlorides and bicarbonates (R. 19). These waters have been drunk and also used for bathing purposes by large numbers of people from colonial times (R. 19–20). They have a recognized medical value and are prescribed by physicians both for bathing and internal use (R. 20).

Commencing in 1911 the State acquired all of the then existing springs (R. 20). Title to all lands from which the springs flowed or spouted was taken and remains in the name of the State (R. 20). Jurisdiction over the springs were transferred in 1930 to the newly created Saratoga Springs Commission, the legislature declaring its purpose to be to develop the Reservation as a state health resort and spa for public health purposes (R. 21). For ten years prior to 1930 waters from the springs were bottled and sold by a private corporation under a lease from the State. (R. 22.) This lease had 15 years to run when the State purchased the lessee's rights, constructed a modern and efficient bottling works and took over the bottling and sale of the waters (R. 22).

The waters bottled and sold consist of three mineral waters and one plain water of high chemical and vegetable purity. (R. 22.) Proceeds from the sales amounted to $104,434.98 for the fiscal year 1933 and $101,675.80 for the fiscal year 1934 (R. 23). In addition to the waters sold, large quantities were consumed on the Reservation free of charge at the springs and at various drink pavilions and upon payment of admission fees, at two drink Halls (R. 23). The sales of the bottled water were made through distributors and retailers and by direct shipment to consumers (R. 23). Advertising amounted to $29,607.98 and $18,392.62 for the fiscal years 1933 and 1934 respectively (R. 24).

In the annual report of the Commission and Authority for the fiscal year 1936, the need for promotion of the spa was stressed, and it was asserted that the average of $30,130.23 per year spent during the past five years for this purpose had been wholly inadequate in comparison with expenditures of other institutions in similar fields (R. 25). The following is an excerpt from the report (R. 25–26):

> White Rock spends $400,000 a year. French Lick Springs spends on Pluto Water and the hotel $300,000 a year. The Greenbrier, at White Sulphur Springs, West Virginia, spent $44,215 last year, and the Homestead at Virginia Hot Springs, $30,000. One hotel at Hot Springs, Arkansas, The Arlington, spent $20,000 in ad-

vertising its baths. The Bernard McFadden "health" hotel at Dansville, N. Y., spent $90,491 last year. Foreign waters and products spent similar sums in our own market. Carlsbad products spent $80,285 last year over the radio alone in promoting the salts derived from the Czecho-Slovakian waters, with an additional $4,875 in magazine advertising. Vichy Celestin Water spent $25,000 in New York City alone.

It must be borne in mind that expenditures at Saratoga have been for the Spa and its waters both, in spite of the fact that they are distinct and should be promoted individually; the Spa offering services and waters being a product. * * *.

None of the watering places or spas referred to above and located in the United States is owned or operated by the Federal Government or by any state, state commission or authority or political subdivision, and the parties know of none which is so operated (R. 28). Several of these privately owned spas have bottled and sold mineral waters to the general public (R. 28).

In addition to the foregoing matters it should perhaps be noted that there are many facilities at the Reservation available to the citizens of New York State and the public generally on equal terms (R. 30). Fees are charged for admission to the drink halls, bath houses, recreation center, and the summer theatre, except for charity treatments administered at the bath houses (R. 30).

The largest items of income are the receipts from admissions to the bath houses and from sales of bottled waters, but the largest item of net income is derived from the lease of the property known as the Gideon Putnam Hotel Sanitarium (R. 31). The Authority also operates a bus line from the City of Saratoga Springs to certain of the baths and facilities located about two miles south of the downtown section of the city and charges fares for such transportation (R. 29, 31). Also located on the Reservation are an administration and research laboratory, and a recreation center with swimming pool, golf course, outdoor gymnasium and other facilities for outdoor recreation (R. 29).

The District Court found as ultimate facts that in bottling for sale and in selling mineral and table waters the State and its agencies embarked in a business which would normally be taxable, that the activities so conducted by the State and its agencies had the characteristics of a business enterprise and that the waters were sold in competition with private waters (R. 40). Accordingly the Court concluded that the State and its agencies were not entitled to immunity from Federal taxation by virtue of the provisions of the Federal Constitution (R. 40). From the judgment in favor of the United States (R. 42–43) an appeal was taken to the United States Circuit Court of Appeals for the Second Circuit (R. 46–

47), which sustained the judgment below (R. 50-54).

ARGUMENT

The decision below is clearly supported by *South Carolina* v. *United States*, 199 U. S. 437; *Ohio* v. *Helvering*, 292 U. S. 360; and *Allen* v. *Regents*, 304 U. S. 439. Those cases establish that when a State[1] engages in a business in competition with private persons it is similarly subject to Federal taxation; and that this result is not affected by the fact that the activity is a means adopted for carrying on a governmental function.[2] See also *State of California* v. *Anglim*, 129 F. 2d 455 (C. C. A. 9th), certiorari denied, 317 U. S. 669.

Petitioners urge as a distinction that in the instant case the State is engaged in the disposition of its natural resources. This case involves no isolated disposition of natural resources but an active business originated by private persons (R. 22). In any event, as the District Court pointed out (R. 38), the natural resources are

[1] While the State was joined as a defendant its precise connection with the matter was in doubt (R. 4). By its answer the State admitted that the other defendants were its agencies (R. 9). It has been stipulated that the Commission and the Authority actually conducted the business (R. 17).

[2] Our conception of a governmental function, of course, does not include the bottling and sale of mineral waters. However, the *Regents* case (304 U. S. at p. 449) makes it plain that the acceptance of such classification would not change the decision.

not being disposed of as such. The mineral waters were put through a bottling process to preserve them and then sold in competition with private waters. The unbottled mineral waters which were given or sold to the public at the Reservation are not involved.

The relationship of the bottling and sale of the mineral waters to the State's program of conservation, health and welfare is no more important than the relationship of the athletic contests to the Georgia program of public education in the *Regents* case, *supra*. Although the admissions tax in that case was payable by the public, the exaction sustained by this Court was a penalty imposed directly upon an instrumentality of the State for failure to collect the tax (304 U. S. 449).

CONCLUSION

There is no conflict. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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No. 83

In the Supreme Court of the United States

OCTOBER TERM, 1944

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, PETITIONERS

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

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OPINIONS BELOW

The opinion of the District Court (R. 22–26) is reported in 48 F. Supp. 15. The opinion of the Circuit Court of Appeals (R. 33–37) is reported in 140 F. 2d 608.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 23, 1944. (R. 37.). The petition for a writ of certiorari was filed May 12, 1944. The petition was granted

on June 12, 1944. (R. 39.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the State of New York and its agencies are entitled to immunity from the federal excise taxes imposed by Section 615 (a) (5) of the Revenue Act of 1932 in respect of certain mineral and table waters bottled and sold by the agencies.

STATUTE AND CONSTITUTIONAL PROVISIONS INVOLVED

Constitution of the United States:

> ARTICLE I
>
> SECTION 8. The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States:
>
> * * * * *

Revenue Act of 1932, c. 209, 47 Stat. 169:

> * * * * *
>
> TITLE IV—MANUFACTURERS' EXCISE TAXES
>
> SEC. 615. TAX ON SOFT DRINKS.
>
> (a) There is hereby imposed—
>
> * * * * *
>
> (5) Upon all natural or artificial mineral waters or table waters, whether car-

bonated or not, and all imitations thereof, sold by the producer, bottler, or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of 2 cents per gallon.

* * * * *

STATEMENT

This is a suit by the United States to collect taxes, interest and penalties assessed on the bottling for sale and sale in closed containers of natural mineral and table waters at a price in excess of 12½ cents per gallon by the Saratoga Springs Commission and the Saratoga Springs Authority during the period June 21, 1932, to May 10, 1934, inclusive. (R. 9–10.)

The Saratoga Springs Commission (hereinafter referred to as the Commission) is a public commission of the State of New York, which was created in 1930 as a temporary commission for a term of seven years and continued in 1937 as a permanent commission. (R. 10.) The Saratoga Springs Authority (hereinafter referred to as the Authority) is a public benefit corporation of the State created in 1933 to take over the management of a State Reservation at Saratoga Springs (hereinafter referred to as the Reservation) by lease from the Commission. (R. 10.) The Authority was established in order to obtain a loan from the Reconstruction Finance Corporation to aid in the further development of the Reservation

for public health purposes in accordance with the declared policy of the State. (R. 10.)

During the period June 21, 1932, to May 10, 1934, inclusive, the Commission and Authority bottled for sale and sold in closed containers certain natural mineral and spring waters at a price in excess of 12½ cents per gallon to various vendees within and without the State. Returns disclosing the amount of tax payable, if due, on the sales made during this period were filed under protest with the Federal Collector of Internal Revenue at Albany, New York. The returns were filed by the Commission for the period June, 1932, to September, 1933, inclusive, and by the Authority for the period October, 1933, to May, 1934, inclusive. (R. 10–11.) A statement was attached to each return that no tax was due upon the ground that the sale of the waters by the State was the exercise of a governmental function. (R. 11.) The taxes in the amounts disclosed by the returns, together with interest and penalties, were assessed by the Commissioner of Internal Revenue and notices and demands for payment were issued upon the proper parties, but no part thereof has been paid. (R. 11–12.)

The waters, the bottling and sale of which gave rise to the instant controversy, came from mineral springs on the Reservation in the vicinity of Saratoga Springs, New York. The waters are char-

acterized by a supersaturation of carbon dioxide gas, and contain in various quantities and combinations, minerals in solution, the most common of which are salt, soda, calcium, magnesium and iron in the form of chlorides and bicarbonates. (R. 12.) These waters have been drunk and used for bathing purposes by large numbers of people from colonial times. (R. 12.) They have a recognized medical value and are prescribed by physicians both for bathing and internal use. (R. 12.)

Commencing in 1911 the State acquired all of the then existing springs. (R. 13.) Title to all lands from which the springs flowed or spouted was taken and remains in the name of the State. (R. 13.) Jurisdiction over the springs was transferred in 1930 to the newly created Saratoga Springs Commission, the legislature declaring its purpose to be to develop the Reservation as a state health resort and spa for public health purposes. (R. 13.) For ten years prior to 1930 waters from the springs were bottled and sold by a private corporation under a lease from the State. (R. 14.) This lease had 15 years to run when the State purchased the lessee's rights, constructed a modern and efficient bottling works and took over the bottling and sole of the waters. (R. 14.)

The waters bottled and sold consist of three mineral waters and one plain water of high chemical and vegetable purity. (R. 14.) Proceeds from the sales amounted to $104,434.98 for the

fiscal year 1933 and $101,675.80 for the fiscal year 1934. (R. 15.) In addition to the waters sold, large quantities were consumed on the Reservation free of charge at the springs and at various drink pavilions and, upon payment of admission fees, at two drink halls. (R. 15.) The sales of the bottled water were made through distributors and retailers and by direct shipment to consumers. (R. 15.) Advertising amounted to $29,607.98 and $18,392.62 for the fiscal years 1933 and 1934 respectively. (R. 16.)

In the annual report of the Commission and Authority for the fiscal year 1936, the need for promotion of the spa was stressed, and it was asserted that the average of $30,130.23 per year spent during the past five years for this purpose had been wholly inadequate in comparison with expenditures of other institutions in similar fields. (R. 16.) The following is an excerpt from the report (R. 16–17):

> White Rock spends $400,000 a year. French Lick Springs spends on Pluto Water and the hotel $300,000 a year. The Greenbrier, at White Sulphur Springs, West Virginia, spent $44,215 last year, and the Homestead at Virginia Hot Springs, $30,000. One hotel at Hot Springs, Arkansas, The Arlington, spent $20,000 in advertising its baths. The Bernard McFadden "health" hotel at Dansville, N. Y., spent $90,491 last year. Foreign waters

> and products spend similar sums in our own market. Carlsbad products spent $80,285 last year over the radio alone in promoting the salts derived from the Czecho-Slovakian waters, with an additional $4,875 in magazine advertising. Vichy Celestin Water spent $25,000 in New York City alone.
>
> It must be borne in mind that expenditures at Saratoga have been for the Spa and its waters both, in spite of the fact that they are distinct and should be promoted individually; the Spa offering services and waters being a product. * * *

None of the watering places or spas referred to above and located in the United States is owned or operated by the Federal Government or by any state, state commission or authority or political subdivision, and the parties know of none which is so operated. (R. 19.) Several of these privately owned spas have bottled and sold mineral waters to the general public. (R. 19.)

In addition to the foregoing matters it should perhaps be noted that there are many facilities at the Reservation available to the citizens of New York State and the public generally on equal terms. (R. 20.) Fees are charged for admission to the drink halls, bath houses, recreation center and the summer theatre, except for charity treatments administered at the bath houses. (R. 20.) The largest items of income

are the receipts from admissions to the bath houses and from sales of bottled waters, but the largest item of net income is derived from the lease of the property known as the Gideon Putnam Hotel Sanitarium. (R. 21.) The Authority also operates a bus line from the City of Saratoga Springs to certain of the baths and facilities located about two miles south of the downtown section of the City and charges fares for such transportation. (R. 20, 21.) Also located on the Reservation are an administration and research laboratory, and a recreation center with swimming pool, golf course, outdoor gymnasium and other facilities for outdoor recreation. (R. 19–20.)

The District Court found as ultimate facts that in bottling for sale and in selling mineral and table waters the State and its agencies embarked in a business which would normally be taxable, that the activities so conducted by the State and its agencies had the characteristics of a business enterprise and that the waters were sold in competition with private waters. (R. 27.) Accordingly the court concluded that the State and its agencies were not entitled to immunity from federal taxation by virtue of the provisions of the Federal Constitution. (R. 27.) From the judgment in favor of the United States (R. 29) an appeal was taken to the Circuit Court of Appeals for the Second Circuit, which affirmed the judgment (R. 33–37).

SUMMARY OF ARGUMENT

The decisions of this Court from *South Carolina* v. *United States*, 199 U. S. 437, to *Allen* v. *Regents of the University System of Georgia*, 304 U. S. 439, establish the principle that a state is not constitutionally immune from federal taxation with respect to activities of a business nature which would otherwise be taxable. This limitation on immunity is a sound one. It represents an accommodation between the right of each state to preserve its government and the power of Congress to levy indirect taxes which shall be uniform. The states are free to engage in enterprises and deal in property of whatever kind, and may promote those activities by local exemptions and subsidies, but may not thereby withdraw sources of national revenue from the power of federal taxation. In addition, the limitation represents a proper allocation of judicial and legislative functions. The judgment whether state activities beyond those which peculiarly belong to the state shall be withdrawn from federal taxation is left to Congress. As a federal legislative problem, it is open to solutions which are not rigid and which take into account relative benefits and burdens, through a legislative process in which the states themselves are represented. Because Congress is a federal legislature, a superficial rule of reciprocal immunity for states and nation would be misconceived, and from the beginning no such

rule has been applied. In many instances, Congress has confirmed the soundness of this view by refraining from taxing states and their instrumentalities to the limit of constitutional power and by waiving the immunity of federal agencies, in whole or part, from state taxation.

The fact that the enterprise here taxed is the sale of property does not render it a function which is constitutionally immune, as the *South Carolina* case, *supra*, demonstrates. Nor is it helpful to describe the activity as a sale of "natural resources". Such a conception is irrelevant to the problem of tax immunity and its proper limits, and the conception would be an impractical one in application. In the present case the resources were acquired by the state only in recent years, and their disposal involves a measure of processing. Thus the present case illustrates the irrelevance and impracticality of a distinction which would in substance be one between extractive industries on the one hand and the furnishing of services or the sale of agricultural and manufactured products on the other.

ARGUMENT

THE BUSINESS OF BOTTLING AND SELLING MINERAL WATERS CARRIED ON BY AGENCIES OF THE STATE OF NEW YORK IS NOT AN ACTIVITY CONSTITUTIONALLY IMMUNE FROM THE APPLICABLE FEDERAL EXCISE TAX

It is unquestioned that the federal excise tax imposed by Section 615 (a) (5) of the Revenue

Act of 1932, *supra*, pp. 2–3, is applicable, as a matter of statutory construction, to the sale by petitioners of the mineral waters which are bottled and sold by them. The sole question is whether the state and its agencies enjoy a constitutional immunity from the tax. The courts below held, without dissent, that under the principles established by the decisions of this Court the constitutional immunity does not extend to activities of the kind in which petitioners are engaged. This conclusion, we submit, is clearly right.

Prior to 1930, the mineral and table waters now bottled for sale and sold by agencies of the State of New York were bottled and sold by a private corporation. In that year, the State purchased the business, constructed a modern bottling works and itself undertook to bottle and sell the waters. No other state has engaged in a comparable activity, similar enterprises being carried on exclusively by private persons. The business involves the continuing use of capital, labor, and management. The processed waters are distributed in the channels of trade throughout the eastern half of the United States with distributors located in many states. The trial court found that the State had "embarked in a business which would normally be taxable" (R. 27). The court also found that the waters "were sold in competition with private waters" and that the undertaking had "the characteristics of a business enterprise" (*ibid.*).

Under the decisions of this Court, early and late, Congress is not precluded by the Constitution from applying to such an activity a general and uniform excise tax. The governing principle was thus stated in *Allen* v. *Regents of the University System of Georgia*, 304 U. S. 439, 451: "When a State embarks in a business which would normally be taxable, the fact that in so doing it is exercising a governmental power does not render the activity immune from federal taxation." While the principle had been suggested previously, it was definitely announced in *South Carolina* v. *United States*, 199 U. S. 437.[1] There the State had established a system of dispensaries for the sale of liquor, which were held liable for federal license taxes imposed on dealers in intoxicating liquors. The State was obviously acting in the interest of the health and morals of its people, and because of the monopolistic feature of the system there was no competition with privately conducted business. Whatever the differences may be between the sale of liquor in that case and the sale of bottled mineral waters in the present case, those differences do not have a constitutional flavor. Indeed, the present case is stronger in that the sale is in competition with similar businesses in New York and in other states, whereas the sale by South Carolina rendered it alone taxable in that State. The *South Carolina* case was

[1] Cf. *United States* v. *Railroad Company*, 17 Wall. 322, 333–335 (dissenting opinion of Justices Clifford and Miller).

followed in *Ohio* v. *Helvering*, 292 U. S. 360, where the distribution system for the sale of intoxicating liquors consisted of stores owned exclusively by a state. In that case, the constitutional question raised by the imposition of the federal excise tax on the sale of liquor was considered so clear that decision was put upon that ground without passing upon the question of the jurisdiction of this Court to entertain the suit.

A similar decision was given in *Helvering* v. *Powers*, 293 U. S. 214, holding that publicly-appointed trustees operating a street railway on behalf of the state were subject to federal income tax because the nature of the activity lay outside the scope of constitutional immunity. And in *Allen* v. *Regents, supra*, the Court held that the State of Georgia was not entitled to immunity from a penalty asserted for failure to collect the federal admissions tax on admissions paid at athletic contests held by state-owned universities, even though the activities were deemed by the local authorities to be an "integral part of the program of public education conducted by Georgia" (p. 449). On the same day that the *Regents* case was decided, this Court was able to state that the "judicial pronouncements marking the boundaries of state immunity * * * definitely establish[ed]" as a guiding principle of limitation that there is excluded from the immunity "activities not thought to be essential to the pres-

ervation of state governments even though the tax be collected from the state treasury." *Helvering* v. *Gerhardt*, 304 U. S. 405, 419.

It is submitted that the limitation thus described and repeatedly applied is a sound one. Its validity rests mainly on two important grounds. First, it is a practical and proper accommodation between the express power of Congress to levy indirect taxes which shall be uniform and the implied right of each state to preserve the existence of its government. Secondly, it represents a sound allocation of functions between the judiciary and the legislature in marking the boundaries of tax immunity of the states. We turn to these considerations.

The application of the doctrine of immunity "must be practical" (*Burnet* v. *A. T. Jergins Trust*, 288 U. S. 508, 516), particularly where, as here, the immunity is an implied one and must be harmonized with the express grant to Congress of the taxing power. Enlargement of state immunity means diminution of the national taxing power and national sources of revenue. The immunity must therefore be limited to the necessity which gave rise to its implication. It was this practical judgment which undoubtedly lay at the basis of the decision in the *South Carolina* case, *supra*. See *Murray* v. *Wilson Distilling Co.*, 213 U. S. 151, 173. The problem, and its resolution, were thus put in *Helvering* v. *Gerhardt*, *supra*, at 417:

> * * * But if every federal tax which is laid on some new form of state activity, or whose economic burden reaches in some measure the state or those who serve it, were to be set aside as an infringement of state sovereignty, it is evident that a restriction upon national power, devised only as a shield to protect the states from curtailment of the essential operations of government which they have exercised from the beginning, would become a ready means for striking down the taxing power of the nation. See *South Carolina* v. *United States*, 199 U. S. 437, 454–455.

The distinction between "strictly governmental" and "proprietary" functions, stemming from the *South Carolina* case, and subsequently phrased in various ways, is simply an effort to describe the balance reached between the claims of the national government for revenue and those of the states for preservation. If the terms used tend to connote a judgment on the wisdom or worthiness of particular undertakings by the states, the terms are indeed unfortunate. But when used in their present context, they mean only that state activities, however appropriate in a period when local governments are impelled to undertake important additional responsibilities, are not constitutionally immune from taxation if they are outside the very limited class of functions which are peculiarly and indispensably carried on by the states. Perhaps the scope of

"strictly governmental" for purposes of tax immunity may be paraphrased in the language of an Australian judge applying the limitation: "* * * the function is not strictly governmental in the sense of being a function essential to all government, a function like the legislative, executive and judicial functions, without which a civilized state cannot be conceived, a function with which the state cannot part." Higgins, J., in *Amalgamated Society of Engineers* v. *Adelaide Steamship Company, Ltd.*, 28 C. L. R. 129, 170.

The limitation of immunity is also, as stated above, a sound allocation of judicial and legislative functions. Precisely because the wisdom of extending the field of state activities is a question for the state legislature, no relevance attaches to that judgment in marking the limits of tax immunity once the narrow field of indispensable state functions has been passed. Constitutional immunity from taxation is not a privilege conferred to encourage or to subsidize enterprises undertaken by the state. Such encouragement and subsidy are a proper subject of state legislation, whether by conferring local tax exemption or by other favored treatment. The Federal Constitution places no bar upon the states in that regard. *Puget Sound Power and Light Co.* v. *Seattle*, 291 U. S. 619. But it will not be suggested that it is for the state legislature to determine whether an activity of the state is to be immune from federal taxation.

That decision rests with Congress and with this Court.

In this aspect, the alternatives are either to increase the area in which by judicial decision state activities are permanently and irremediably withdrawn from federal taxation, or to leave the largest possible scope for that determination to be made by Congress, with that opportunity for change, for consideration of benefits and burdens, and for constructive solutions, which is characteristic of the legislative process. Thus viewed, the limitation laid down in the *South Carolina* case has special merit. This factor, too, was pointed out in the *Gerkardt* case, *supra,* at 416:

> * * * the people of all the states have created the national government and are represented in Congress. Through that representation they exercise the national taxing power. The very fact that when they are exercising it they are taxing themselves, serves to guard against its abuse through the possibility of resort to the usual processes of political action which provides a readier and more adaptable means than any which courts can afford, for securing accommodation of the competing demands for national revenue, on the one hand, and for reasonable scope for the independence of state action, on the other.

It is because Congress is a federal legislature that, as was appreciated by Chief Justice Mar-

shall in *McCulloch* v. *Maryland*, 4 Wheat. 316, 435–436, problems of intergovernmental tax immunity cannot be solved by a superficial rule of reciprocity.[2] It is not to be expected that individual states will waive claims to immunity in the interest of the national revenue; Congress, on the other hand, can be expected to, and does frequently, waive the immunity of federal agencies. By the same token, the states are without

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[2] Compare Bradley, J., dissenting, in *Collector* v. *Day*, 11 Wall. 113, 128–129:

"* * * The taxation by the State governments of the instruments employed by the general government in the exercise of its powers, is a very different thing. Such taxation involves an interference with the powers of a government in which other States and their citizens are equally interested with the State which imposes the taxation. * * * I cannot but regard it [the decision] as founded on a fallacy, and that it will lead to mischievous consequences. I am as much opposed as any one can be to any interference by the general government with the just powers of the State governments. But no concession of any of the just powers of the general government can easily be recalled."

Mr. Justice Frankfurter, concurring, in *Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466, 489, stated:

"* * * The seductive *cliché* that the powers to tax involves the power to destroy was fused with another assumption, likewise not to be found in the Constitution itself, namely the doctrine that the immunities are correlative—because the existence of the national government implies immunities from state taxation, the existence of state governments implies equivalent immunities from federal taxation. When this doctrine was first applied Mr. Justice Bradley registered a powerful dissent, the force of which gathered rather than lost strength with time. *Collector* v. *Day*, 11 Wall. 113, 128."

power to confer immunity upon their own activities beyond that which would otherwise be implied from the Constitution; while Congress may declare an immunity which might not be held to exist in the silence of Congress. See *Pittman* v. *Home Owners' Loan Corp.*, 308 U. S. 21; *Federal Land Bank of St. Paul* v. *Bismark Lumber Co.*, 314 U. S. 95. It is signficant that at the time when this Court removed the salaries of government employees from the sphere of immunity, the Court took occasion to state: "That the two types of immunity [state and national] may not, in all respects, stand on a parity has been recognized from the beginning, *McCulloch* v. *Maryland, supra,* 435–436; and possible differences in application, deriving from differences in the source, nature and extent of the immunity of the governments and their agencies, were pointed out and discussed by this Court in detail during the last term. *Helvering* v. *Gerhardt, supra,* 412–413, 416." *Graves* v. *New York ex rel O'Keefe,* 306 U. S. 466, 478.

There are numerous instances in which Congress has in fact refrained from taxing the states and their instrumentalities, and has waived the immunity of federal agencies, wholly or partly, from state taxation. The federal income tax law does not apply to states and their agencies, and no effort is made to tax whatever income accruing to them may be constitutionally reached. See G. C. M. 14407, XIV–1 Cum. Bull. 103.

The local taxation of national banks under congressional permission, is well known (R. S. 5219). When the National Government took over the operation of the railroads during the last war, provision was made for the continuance of state taxation. 40 Stat. 451, 458. A recent governmental study enumerates 23 statutes authorizing the imposition of taxes on federally-owned real estate in the same manner and to the same extent as on privately-owned property; 17 statutes authorizing contributions from the revenues of federal agencies to states and counties based on a percentage of receipts; 7 statutes authorizing such contributions to be made by agreement or other arrangement; and 36 bills relating to the taxation of federal real estate introduced in the 77th Congress alone. House Document 216, 78th Cong., 1st sess. (*Federal Contributions to States and Local Governmental Units with respect to Federally Owned Real Estate*). Not merely the number of such statutes, but the factors entering into the legislative judgment, are significant.[3]

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[3] For example, in authorizing agreements for payments to local authorities in lieu of taxes on federal slum-clearing and low-cost housing projects, Congress provided: "Such sums shall be fixed in such agreement and shall be based upon the cost of public or municipal services to be supplied for the benefit of such project or the persons residing on or occupying such premises, but taking into consideration the benefits to be derived by such State or subdivision from such projects." 49 Stat. 2026.

The experience with respect to the Tennessee Valley Authority is also illuminating. David E. Lilienthal, *TVA:*

To obtain tax immunity for commercial undertakings, no less than to obtain authority to tax nationally owned property or activities, the appropriate course for the states is through "peti-

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Democracy on the March (1944) 159, describing the amendment of the statute in 1940, states:

> TVA made an exhaustive analysis of the facts respecting local tax problems as a result of TVA property purchases, the prospects for the future, the benefits received by the region from federal funds. The details of the varying tax laws of several different states were analyzed closely. Then TVA representatives conferred with the governors and fiscal officers of all the states, of many counties with peculiarly difficult problems, with tax consultants, and with federal tax officials. As a result a measure was drafted which embodied principles that TVA as a national agency could recommend. And, although far short of the original claims of local tax bodies, its fairness led all the states to concur. After exhaustive Congressional committee hearings, the bill as recommended by the TVA and agreed to by the states was passed. Under this law TVA has paid, to the end of the fiscal year 1943, out of its power revenues, a total of $5,320,000 in tax payments to states and counties of the valley; in the single fiscal year ended June 30, 1943, the total of these payments was about two million dollars.

See also Durisch and Macon, *Payments in Lieu of Taxes by the Tennessee Valley Authority*, 3 Journal of Politics 318; Edelman, *Public Ownership and Tax Replacement by the TVA*, 35 Am. Pol. Sci. Rev. 727; Prichett, *The Tennessee Valley Authority* (1943) 111–115; Ransmeier, *The Tennessee Valley Authority* (1942) 72–76.

The presence or absence of what may be called this "inner check" on legislative action is important also in such fields as the protection of minorities and the taxation by the states of interstate commerce. Cf. *South Carolina Highway Dept.* v. *Barnwell Bros., Inc.*, 303 U. S. 177, 185, n. 2; *McGoldrick* v. *Berwind-White Coal Mining Co.*, 309 U. S. 33, 45, n. 2.

tion to the Federal Congress, which also is their Congress." *United States and Mesta Machine Co.* v. *County of Allegheny*, 322 U. S. 174, 191.*

It is, of course, not a doctrine peculiar to taxation that the immunity of states is not perfectly symmetrical with the immunity of the National Government. Congress may provide for the priority of debts due to the United States, even as against claims of the state. *United States* v. *Fisher*, 2 Cranch 358, 397. Congress may tax imports of a state acquired for governmental purposes, *Board of Trustees of the University of Illinois* v. *United States*, 289 U. S. 48, but the states may not levy an inspection fee upon goods brought into the state by the Federal Government, *Mayo* v. *United States*, 319 U. S. 441. The National Government may condemn state-owned land, *Oklahoma* v. *Atkinson Co.*, 313 U. S. 508, 534, but the states may not condemn federally owned land without the consent of Congress, *Minnesota* v. *United States*, 305 U. S. 382, 387.

It is contended, however, that in the present case there is immunity because "it is the essence of sovereignty for a state to be able to dispose of its property" (Brief for the State, p. 12).

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* Cf. Ernst Freund, *Standards of American Legislation* (1917) 281: "If the doctrine of reciprocal exemption sounds plausible in logic, in practice it works inequitable and sometimes intolerable results. It furnishes another illustration of a judicial doctrine that for constructive legislative purposes ought to be rejected."

Petitioners recognize that for purposes of this case their contention must apply to "such property, whether originally owned or acquired with time" (*ibid.*), since it was not until recent years that the source of the mineral waters came into state ownership. But this contention would in substance overrule the *South Carolina* case and the *Ohio* case, *supra*, which involved the sale of liquors owned by the state and distributed in the performance of its public responsibilities. The contention would, moreover, draw an irrelevant distinction between the sale of property on the one hand and the sale of services on the other, such as the furnishing of transportation involved in the *Powers* case. Petitioners' contention may perhaps be limited to the sale of what are deemed by them to be "natural resources". As a criterion critical for constitutional purposes, this is highly indefinite. Thus the state itself at one point observes that "The number of natural resources is not large" (p. 14), and at another point asserts: "Land, water, oil, coal, gold, gravel in river beds, are but a few of the natural resources that the states have sold" (p. 12). The suggested classification might draw an anomalous constitutional line between the extractive industries and agricultural or manufacturing enterprises; it would presumably require, also, the drawing of distinctions dependent on the degree of processing to which the "resources" are subjected prior to sale.

The states have plenary power to acquire and dispose of all types of raw materials and other property. Cf. *Jones* v. *Portland*, 245 U. S. 217; *Green* v. *Frazier*, 253 U. S. 233. To introduce a legal concept of natural resources to enlarge the sphere of tax immunity would be, aside from its impracticality, irrelevant, uncalled for from the standpoint of protecting state functions, and unsound from the standpoint of maintaining the available sources of federal revenues.

Apparently recognizing that the suggested criterion is vulnerable, the state finally narrows its contention to apply solely to the sale of natural resources in connection with a "larger program". It says that "to grant immunity in the case at bar does not necessarily require immunity when a state engages in a wholesale disposition of its natural resources, unrelated to any particular program" (p. 16). Once again, it must be recalled that it is not for the federal courts to decide whether commercial selling enterprises engaged in by a state have greater or less claim to immunity because of their asserted relation or lack of relation to a larger public program. It should also be remarked that, so far as the other activities of the state at Saratoga Springs are concerned, some of them would admittedly be taxable (Pet. 16), and the relation to them of the sale of bottled waters throughout the eastern states is simply the providing of additional funds. The decision in *Allen* v. *Regents*, as well as in the South Carolina case, deci-

sively rejected the argument that the provision of funds for any state purpose through a commercial enterprise is a basis for tax immunity. This proposition answers, likewise, the use made by petitioners (Brief for State, pp. 9, 12–13) of the opinions in *Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393; *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279; and *Helvering* v. *Mountain Producers Corp.*, 303 U. S. 376, the first of which has been overruled and the other two of which held the income in question taxable. The opinion in the first case stressed the governmental character, not of the lease of oil lands by the State, but of the use of the royalties for school purposes (285 U. S. at 398, 400), an analysis rejected in the later *Regents* case. The language relied on in the second case was, of course, dictum, and in the third case only a form of stating the question, and in neither could the opinion have meant to sanction the withdrawal from federal taxation of the sale of property by virtue of its acquisition and disposal by the state in lieu of private ownership and distribution.

As stated above, the Constitution gives full scope to the States and their subdivisions to expand and foster public enterprises in accordance with local policies and by many means, but not, unless Congress so provides, at the expense of the general, non-discriminatory taxing power of the national government, upon whose sources of revenue the general welfare is dependent.

CONCLUSION

For the reasons stated, the judgment below should be affirmed.

Respectfully submitted.

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No. 5

In the Supreme Court of the United States

OCTOBER TERM, 1945

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, PETITIONERS

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

SUPPLEMENTAL BRIEF FOR THE UNITED STATES ON REHEARING

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On October 8, 1945, the Court entered an order herein requesting counsel, "without restricting their argument in any other respect", to consider the following questions:

1. May Congress constitutionally include for taxation in a generally applicable taxing act any state property or activity or the income derived by the state from them, or any other source, so long as the tax does not discriminate against the state, or so long as the tax is not laid on the interest taxed, merely because it is that of a state—and if income of a private person from a like source may be constitutionally taxed?

2. To what extent may a state, by enlarging its property ownership or its activities, withdraw from the reach of the federal taxing power property and income which are normally subject to federal taxation when owned or received by private persons? See *United States* v. *California*, 297 U. S. 175, 184, 185, and cases cited.

We think that the answer to the first question is yes, and to the second that a state may not to any extent so withdraw property and income from the reach of the federal taxing power. Since the second question suggests a more moderate limitation of the doctrine of immunity than does the first question, we shall deal with it at the outset.

I

In our original brief we maintained that this case comes squarely within the scope of *South Carolina* v. *United States*, 199 U. S. 437, and the cases which have followed it. *Ohio* v. *Helvering*, 292 U. S. 360; *Helvering* v. *Powers*, 293 U. S. 214; *Allen* v. *Regents of the University System of Georgia*, 304 U. S. 439. Those cases made it clear, in our view, that the immunity doctrine, even in the broadest scope to which it has ever been extended, does not apply to state activities of the character here involved.

We pointed out that any limitation on the federal taxing power other than those contained in the Constitution itself—that direct taxes shall be levied according to population and that indirect

taxes shall be uniform—rests on implication; that the doctrine of immunity of states from federal taxation has been deemed to rest on the necessity of preserving our dual form of Government; and that in accommodating the express power of national taxation and the asserted immunity, the latter must not be carried beyond the necessity which alone has given rise to its implication. We sought to show that the principle of the *South Carolina* case was a relatively early recognition of this practical need for limiting the immunity doctrine so that in the name of protection against the destruction of state governments the taxing power of the National Government would not itself be impaired or destroyed. An appropriate limitation of the immunity doctrine had been particularly called for, we insisted, because immunity founded on an assumed constitutional basis is irremediable by Congress, whereas taxability as a matter of constitutional law leaves open the conferring of exemption by act of Congress in which the states are represented, and "which also is their Congress," *United States* v. *Allegheny County*, 322 U. S. 174, 191. Thus the principle of the *South Carolina* case, from which there has been no departure in the whole history of the judicial treatment of immunity, stands as a recognition of the perils of immunity, a recognition that long antedated the notable series of decisions by which this Court has retreated from the immunity doctrine in numerous additional aspects.

While admittedly the appellations "governmental" and "proprietary" may be inapt to express the limitation in the *South Carolina* case and succeeding cases, a limitation was nonetheless imperative, in somewhat the same sense that state courts have found a similar limitation imperative to place bounds on the rule of state and municipal immunity in tort. The real question is whether any immunity whatever should be retained, or whether, as New York has done in the case of tort liability (see Pet. Br. on reargument, p. 43, n.), the remnant of immunity should be abandoned. That question we discuss below. At this point we shall not repeat the argument in our original brief, to which we adhere, that under any classification of activities which is appropriate as a qualification of immunity, or, to put it otherwise, as an accommodation of the federal revenue power and the preservation of the states, the sale of bottled mineral water throughout half the country in active competition with private brands is not shielded by the Constitution from a non-discriminatory federal tax.[1]

[1] We dealt in our original brief with the state's contention that the disposal of a natural resource is not within the scope of the *South Carolina* case (see our brief, pp. 23–24). Apart from questions of the meaning of "natural resource" and the point at which processing of a commodity goes beyond mere disposal, the suggested category would introduce for constitutional purposes a curious distinction between the extractive industries on the one hand and agriculture or manufacturing on the other. The state now apparently substi-

The second question put by the Court focuses attention on a significant factor supporting the principle of the *South Carolina* case. That case was explained in *Murray* v. *Wilson Distilling Company*, 213 U. S. 151, 173, as "concerned with the power of a State, by virtue of its legislation in regard to the sale and consumption of liquor, to destroy a preexisting right of taxation possessed by the Government of the United States." We do not understand that under this reasoning it would be necessary to show that the precise excise tax in question was levied prior to the state's embarking upon the enterprise in question, and in any event a tax like that here involved was so levied (Pet. Br. on Rearg., p. 48).

This Court has observed that the sovereign taxing

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tutes for natural resources the broader concept of "public services" (Brief on reargument, p. 42). It is not clear why the sale of alcoholic liquor by a state dispensary, or the furnishing of street car transportation, would not be a public service, thus invalidating rather than distinguishing the decisions in the *South Carolina*, *Ohio*, and *Powers* cases. In any event, very few business enterprises, those carried on by private no less than public agencies, today forego description as "public services." The Court will not, we believe, seek to resolve constitutional issues by importing a phrase having an ominous resemblance to "business affected with a public interest."

Nor does it seem helpful to point out (Pet. Br. on reargument, p. 20) that the bottled mineral water is not suitable for use in conjunction with alcoholic liquors. The question whether the mineral waters can be legally assimilated to alcoholic beverages does not depend upon whether the two may be palatably mixed in a glass.

power "would be unduly curtailed if either by extending its activities could withdraw from the taxing power of the other subjects of taxation traditionally within it." *United States* v. *California*, 297 U. S. 175, 184, citing *Helvering* v. *Powers*, *supra*; *Ohio* v. *Helvering*, *supra*; and *South Carolina* v. *United States*, *supra*, all cases dealing with federal taxation of state activities. Again, it was said in *Helvering* v. *Gerhardt*, 304 U. S. 405, 417:

> * * * But if every federal tax which is laid on some new form of state activity, or whose economic burden reaches in some measure the state or those who serve it, were to be set aside as an infringement of state sovereignty, it is evident that a restriction upon national power, devised only as a shield to protect the states from curtailment of the essential operations of government which they have exercised from the beginning, would become a ready means for striking down the taxing power of the nation. See *South Carolina* v. *United States*, 199 U. S. 437, 454–455.

The latter passage puts the principle in terms both of "essential" operations of government and historic performance by the state. The important point is that if a non-discriminatory federal tax is forbidden to be laid on a state activity lest the coexistence of the states be threatened, the area of such immunity should be kept at a minimum, for the immunity can only be rationalized as growing out of an abundance

of caution; and as caution and the activities of the state become more and more abundant the sources of federal revenue and the scope for congressional adjustment of competing interests become more paltry.

II

Probably no more unfortunate chapter in the history of constitutional adjudication can be found than the rise and decline of the doctrine of implied immunity of state instrumentalities from federal taxation. Many applications of the doctrine have now been rectified by the overruling of decisions, including that in *Collector* v. *Day*, 11 Wall. 113, in which the doctrine took its origin.[2] The guiding principle in limiting the doctrine of immunity has been that it rests, as has been stated above, on an implied necessity to preserve the existence of the states, and "Springing from that necessity it does not extend beyond it." *Board of Trustees* v. *United States*, 289 U. S. 48, 59. The question remains whether the Court should not move full circle and disavow the necessity for the doctrine, save as it may protect states against exactions which are discriminatory or which are laid on them because they are states. This is the substance of the first question put by the Court.

When the doctrine of immunity of state instrumentalities was announced in 1870 in *Collec-*

[2] See the cases cited in *United States* v. *Allegheny County*, 322 U. S. 174, 177, n. 2.

tor v. *Day*, Mr. Justice Bradley expressed this disagreement and these apprehensions (11 Wall. at 128–129):

> I cannot accede to the doctrine that the general government is to be regarded as in any sense foreign or antagonistic to the State governments, their officers, or people; nor can I agree that a presumption can be admitted that the general government will act in a manner hostile to the existence or functions of the State governments, which are constituent parts of the system or body politic forming the basis on which the general government is founded. The taxation by the State governments of the instruments employed by the general government in the exercise of its powers, is a very different thing. Such taxation involves an interference with the powers of a government in which other States and their citizens are equally interested with the State which imposes the taxation. In my judgment, the limitation of the power of taxation in the general government, which the present decision establishes, will be found very difficult of control. Where are we to stop in enumerating the functions of the State governments which will be interfered with by Federal taxation? If a State incorporates a railroad to carry out its purposes of internal improvement, or a bank to aid its financial arrangements, reserving, perhaps, a percentage on the stock or profits, for the supply of its own treasury, will the bonds

> or stock of such an institution be free from Federal taxation? How can we now tell what the effect of this decision will be? I cannot but regard it as founded on a fallacy, and that it will lead to mischievous consequences. I am as much opposed as any one can be to any interference by the general government with the just powers of the State governments. But no concession of any of the just powers of the general government can easily be recalled. I, therefore, consider it my duty to at least record my dissent when such concession appears to be made. An extended discussion of the subject would answer no useful purpose.

The subsequent history of the doctrine has amply confirmed the soundness of Justice Bradley's position. If anything made clear by the evolution of the doctrine, it is that it was misconceived as a means of preserving the existence of the states and has served to curtail the legitimate demands of the National Government. It is anomalous to single out the non-discriminatory taxing power of the Federal Government as inherently a peculiar threat to the existence of the states, and consequently a power from which certain state functions are immune, while at the same time sustaining the application of nondiscriminatory Federal regulatory measures of all sorts to the states and state-conducted enterprises. Cf. *United States* v. *California*, 297 U. S. 175.

The anomaly is illustrated by comparing customs duties and internal revenue taxes as applied to the states. During the long period when customs duties provided our principal source of national revenue, it apparently occurred to no one that to lay the duties on the states as importers was a constitutionally forbidden threat to the existence and functions of the states. Not until a very recent date was there a challenge to this familiar subjection of the states to the obligation to pay a federal tax. "It is sufficient to say that only in recent years has any question been raised by state officials as to the authority of Congress to impose duties upon their imports." *Board of Trustees* v. *United States*, 289 U. S. 48, 60. It is true that the obligation to pay was there sustained on the reasoning that tariff duties are a form of regulation of commerce, to which states are subject uniformly with others; but no good reason is perceived why a different approach should be taken when the impost is laid solely under the taxing power. The Constitution does not classify the powers of the National Government in a hierarchy of importance. It would be unwarranted to infer that uniformity in the imposition of customs duties is more vital than uniformity in the imposition of internal revenue taxes. Excise taxes, like customs duties, are levied on carefully chosen subjects, with a view not merely to the collection of revenue but to the effect on the econ-

omy and on competition. Immunities introduce distortions in the Congressional design in either case.

Another illustration may be ventured, in the field of social security taxation. The Carriers Taxing Act, providing a system of retirement pensions for railroad workers, may be validly applied to a state as employer, whether on the ground that it represents an exercise of the commerce power or that the activity of the state falls within the South Carolina case. *California* v. *Anglim*, 129 F. 2d 455 (C. C. A. 9), certiorari denied, 317 U. S. 669. Where the employment is not of a similar character, does the Constitution forbid inclusion of employment by the state as a subject of social security taxation? Must the state's payroll as a measure of the tax be winnowed so that, for example, the employer's tax may embrace a clerk or carpenter when he works in the railroad or liquor department but not when he works in the division of parks or archives?[3] Social security taxation rests on the unity and continuity of a human life and the fluidity of employment.

[3] The problem is not academic. In connection with proposals to enlarge the coverage of the Federal Social Security Act, the Chairman of the Social Security Board has estimated that about half of the state and local government employees, or one and a half million workers, are not covered by retirement systems. See Altmeyer, *Social Security for State and Local Government Employees*, Social Security Bulletin, April 1945, p. 4.

Surely to make the cessation and resumption of coverage depend on changes in employment of the kind indicated would have as serious effect on the aims of social security legislation as immunity of the states from customs duties would have had on the objectives of the tariff, and with as little relation to the maintenance of the states.

From the standpoint, too, of benefit and protection conferred by the taxing authority, there is no basis for state immunity. Apart from direct financial outlays such as grants in aid, the National Government obviously confers important benefits on the states no less than on private persons. This is particularly evident where the state is in competition, as here, with private enterprise. The benefit of federal administration of trade-mark and unfair-competition legislation, pure food and drug laws, adequate and economical interstate transportation, and all the host of governmental safeguards for business enterprises, operate in the interest of the state no less than of its taxpaying competitors.

There remains to be considered the argument of reciprocity. To this argument there are several answers. In the first place, as pointed out in our original brief (p. 22), no rule of reciprocity has been thought to exist in the field of regulation, or of condemnation, or of priority of debts. In the second place, true reciprocity is not achieved by conferring absolute immunity on

state activities. Such a reciprocity is more verbal than real. This is true because in the converse field, that of taxation of federal activities by the states, Congress has power, which it has freely exercised, to permit taxation of federal activities by the states. (See our original brief, pp. 19–21.) There is no similar opportunity for Congressional action if immunity of the states is established as a constitutional principle. Reciprocity is a problem not of verbal formulas but of practical adjustments. That is to say, it is a legislative problem.

The Court seems clearly to have come to this view with respect to the question of the validity of state taxation in its relation to the Federal Government. There is an area within which immunity for the Federal Government is implied from the Constitution, but Congress has the power to waive even that immunity. *United States* v. *Allegheny County*, 322 U. S. 174, 189–191; *Mayo* v. *United States*, 319 U. S. 441, 446. On the other hand, many decisions recognize the power of Congress to extend the federal immunity beyond the limits within which it would be implied from the Constitution. *Mayo* v. *United States, supra; Smith* v. *Davis*, 323 U. S. 111, 114, fn. 4, 115; *Cleveland* v. *United States*, 323 U. S. 329, 333; see also the dissenting opinion of Mr. Justice Frankfurter in *United States* v. *Allegheny County, supra*, p. 196. This leaves Congress free to consider the numer-

ous, varied and complex factors which must necessarily enter into the determination of such a problem, to consider the burdens and benefits flowing from immunity *vel non*, and to strike a balance between the needs of state and nation—a balance which, because of the flexibility of the legislative process, may be adjusted from time to time to reflect changes in the underlying factors. The judgment thus reached is one made by a body representative of each and all of the states so that it constitutes, in a very real sense, the judgment of the states themselves.

We respectfully submit that the same approach should characterize the judicial treatment of the other aspect of the immunity problem—the relationship of state and nation with respect to the effects of a federal tax. This, too, is in its essentials a legislative problem which needs resolution by the national legislature in each instance, for it requires an appraisal of factors of the same nature as are involved in the problem of federal immunity—an appraisal which is not properly part of the judicial function. And Congress should manifestly have the broadest possible area within which to act.[4]

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[4] "Reciprocity between the states and the nation is essential to offset or to minimize one of the evils of the immunity doctrine." Yet it may be suggested that in observing the balance between state and nation, consideration should be given to the heavy national expenditures for what used to be deemed primary state concerns and to the state compensations from sales and gross receipts taxes and from inclusion of federal

The truth is that the preservation of the states by immunity from non-discriminatory taxation has been an *ignis fatuus* which has led nowhere but to confusion, collision and retreat. It may be ventured that nothing would have been lost and much gained if the courts had treated the problem from the beginning as a political question. Cf. *Georgia* v. *Stanton*, 6 Wall. 50; *Kentucky* v. *Dennison*, 24 How. 66; *Ohio* v. *Akron Park District*, 281 U. S. 74, 79–80; *Coleman* v. *Miller*, 307 U. S. 433, 450–456.

In any event we submit that the only federal tax which could lend itself as a means of achieving the destruction of the states, and therefore the only federal tax which in any circumstances should ever be held to be constitutionally prohibited, is one which would discriminate against the states as states. Thus a tax which either in form or effect singled out the privilege of being governor of a state, or judge in a state court of record, or the convening of state legislatures, might be the kind of a tax which could be used as a device to terminate the existence of the states. But a non-discriminatory income tax which the governor and the judge must pay in common with all the other citizens of the country, does not involve any such danger. *Helvering* v. *Gerhardt*, 304 U. S. 405; *Graves* v. *New York ex*

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bond interest in the measure of corporate excises." See Powell, *The Remnant of Intergovernmental Tax Immunities*, 58 Harv. L. Rev. 757, 795.

rel. O'Keefe, 306 U. S. 466; *Baker* v. *Commissioner*, 149 F. 2d 342 (C. C. A. 4), certiorari denied, October 8, 1945. Any non-discriminatory tax on state property or a state activity or state income would be no greater threat.

Unless the tax is one which singles out the basic functions which are inherent in the concept of a state and which only a state can perform, it does not constitute a menace to the continued existence of the states. This was the thought in *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 158, when the Court referred to "The exercise of such rights as the establishment of a judiciary, the employment of officers to administer and execute the laws" as illustrative of the state functions which cannot be reached by the federal taxing power. This was also the thought of Higgins, J., of Australia, in *Amalgamated Society of Engineers* v. *Adelaide Steamship Co.*, 28 C. L. R. 129, 170, quoted on page 16 of our original brief.

The petitioners observe that states have pioneered in many fields of public control and public ownership. No one would detract one iota from the achievements of the states in this regard. No one would deny the right of a state to subsidize such endeavors by tax exemption from local taxation or by other means. *Puget Sound Power and Light Company* v. *Seattle*, 291 U. S. 619. No one would deny the right of Congress to exempt such endeavors of a state from federal

taxation, as has been done, for example, in the case of publicly owned power plants.[5] But our question is whether the Constitution requires Congress and the people of all the other states to subsidize such endeavors by granting immunity from taxes laid on comparable private endeavors or income. A judgment whether or not to confer such a subsidy is one upon which the people of all the other states are entitled to have a voice, and they may have that voice only if it is recognized that the problem is one for Congress. Each state is left free to determine for itself the desirability of engaging in a particular activity. But it may not by unilateral action require the Federal Government,

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[5] Section 3411, Int. Rev. Code, imposes a tax on the sale of electrical energy for domestic or commercial consumption. Subsection (c) provides: "No tax shall be imposed under this section upon electrical energy sold to the United States or to any State or Territory, or political subdivision thereof, or the District of Columbia. None of the provisions of this section shall apply to publicly owned electric and power plants, or to electric and power plants or systems owned and operated by cooperative or nonprofit corporations engaged in rural electrification. * * *"

The states enjoy numerous exemptions under the Internal Revenue Code. E. g., Sec. 1808 (a) (documents tax); Sec. 2406 (retailers excise taxes); Sections 2551 (c) and 3222 (b) (narcotics taxes); Sections 2700 (b) (1), 2721 and 3262 (firearms taxes); Section 3466 (a) (communications taxes); Sections 3469 (f) and 3475 (b) (transportation tax); Section 3540 (j) (use tax on motor vehicles and boats). The Federal income tax is construed administratively as not applying to the states. G. C. M. 14407, XIV–1 Cum. Bull. 103.

The Civil War apportioned tax on land exempted state-owned property. 12 Stat. 292, 297, c. 45, sec. 13.

and therefore the other states, to bear a part of the cost of the enterprise in the form of tax exemption.

It is our position that the Constitution is neutral, as it is silent, on the question of state ownership; that such ownership may be, but need not be, given special treatment in general federal revenue laws as in federal regulatory laws; and that such ownership or activities are protected by virtue of the Constitution only against hostile or discriminatory treatment by the National Government.

CONCLUSION

The judgment below should be affirmed.

Respectfully submitted.

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Supreme Court of the United States

OCTOBER TERM, 1945

Supreme Court, U. S.
FILED
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No. 5

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,
Petitioners,

vs.

UNITED STATES OF AMERICA.

BRIEF OF THE CITY OF NEW YORK AND NATIONAL INSTITUTE OF MUNICIPAL LAW OFFICERS, *AMICI CURIAE.*

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Supreme Court of the United States

OCTOBER TERM, 1945

No. 5

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY,

Petitioners,

against

UNITED STATES OF AMERICA.

BRIEF OF CITY OF NEW YORK AND NATIONAL INSTITUTE OF MUNICIPAL LAW OFFICERS, *AMICI CURIAE.*

Preliminary Statement

This joint brief is submitted on behalf of the City of New York and by the National Institute of Municipal Law Officers on behalf of 415 municipalities throughout the country. The law officers of 12 of the country's leading cities have joined in the brief, as representatives of the 415 member cities of the Institute.

Questions Presented

The broad question asked by the Court is whether the Federal government may constitutionally tax any state property, activity or income. It is manifest that the question posed reaches down to and touches the very foundations of the constitutional structure of our country.

We propose to demonstrate that the proper answer to the question is that state property, activities and income,

regardless of their nature or source may not properly be taxed by the Federal government. We propose that this Court return to the basic doctrine of sovereign immunity of states from federal interference by taxation and reject the limitation upon that doctrine which lies in the theory adopted by the Court in deciding *South Carolina* v. *U. S.*, 199 U. S. 437 (1905), and those cases which have in one form or another restated the views expressed in that opinion.*

Outline of Argument

It is our intention in this Brief to demonstrate:

The doctrine of inter-governmental tax immunity is basic in our form of constitutional government. The immunity of State instrumentalities of government from Federal taxation and the immunity of the Federal instrumentalities of government from State taxation are necessarily reciprocal. This immunity proceeds from the circumstance that both the State and the Federal governments are sovereign in their spheres. The *South Carolina* case represents a departure from this principle; its rule is contrary to basic constitutional law and, as a necessary result, so confusing and lacking in precision as to require its abandonment.

Since Federal instrumentalities, regardless of their nature, are immune from State taxation so, under the Constitution, State instrumentalities, regardless of their nature, are similarly immune from Federal taxation.

We shall not consider here whether the Federal government may levy taxes upon incomes received by individuals from states and their instrumentalities nor shall we consider

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* Since the answer we propose to Question "1" framed by the Court in its order for reargument is an unqualified negative, we do not reach Question "2" for consideration. The answer to the latter question is implicit in that which we have made to the former.

whether persons receiving goods or services from states and their instrumentalities may be taxed upon them. These matters pose a problem not presented by the questions framed by the Court in this case.

ARGUMENT

The doctrine of inter-governmental tax immunity is basic in our form of constitutional government. The immunity of State instrumentalities of government from Federal taxation and the immunity of the Federal instrumentalities of government from State taxation are necessarily reciprocal. This immunity proceeds from the circumstance that both the State and the Federal governments are sovereign in their spheres. The *South Carolina* case represents a departure from this principle; its rule is contrary to basic constitutional law and, as a necessary result, so confusing and lacking in precision as to require its abandonment.

Since Federal instrumentalities, regardless of their nature, are immune from State taxation so, under the Constitution, State instrumentalities, regardless of their nature, are similarly immune from Federal taxation.

(1)

Prior to 1905 this Court repeatedly stated that state instrumentalities and their activities, regardless of their nature, were immune from federal taxation (*U. S.* v. *Railroad Company,* 17 Wall. 322 (1873) and cases cited; *Van Brocklin* v. *Tennessee,* 117 U. S. 151 (1886) and cases cited; *Veazi Bank* v. *Fenno,* 8 Wall. 533 (1869) and cases cited. See also Cooley on *Constitutional Limitations* (2 Ed.) pp. [532] *et seq.*, *U. S.* v. *Owens,* 100 Fed. 70 (D. C., E. D. Mo. 1900); *State* v. *Garten,* 32 Ind. 1 (1869)).

Similarly, this Court held, as it has done to this very day, that the converse of that proposition is true and that Federal instrumentalities and their activities are immune

from State taxation regardless of their nature. *McCulloch* v. *Maryland*, 4 Wheat. 316 (1819); *Maricopa County* v. *Valley Bank*, 318 U. S. 357 (1943) and cases cited; *Mayo* v. *U. S.*, 319 U. S. 441 (1943) and cases cited; *U. S.* v. *Allegheny County*, 322 U. S. 174 (1944) and cases cited; *Cleveland* v. *U. S.*, 323 U. S. 329 (1945) and cases cited.

Since *McCulloch* vs. *Maryland*, 4 Wheat. 316 (1819) the fundamental doctrine that the federal government is immune from state taxation and, reciprocally, the state governments are immune from federal taxation has never been questioned in principle.*

The foundation of the rule exempting states from federal taxation was stated by Mr. Justice NELSON in *Collector* vs. *Day*, 11 Wall. 113, 124-5 (1870):

> "The general government, and the States, although both exist within the same territorial limits, are separable and distinct sovereignties, acting separately and independently of each other, within their respective spheres. The former, in its appropriate sphere, is supreme; but the States within the limits of their powers not granted, or, in the language of the tenth amendment, 'reserved' are as independent of the general government as that government within its sphere is independent of the States. * * * Such being the separate and independent condition of the States in our complex system, as recognized by the Constitution, and the existence of which is so indispensable, that, without them, the general government itself, would disappear in the family of nations, it would seem to follow, as a reasonable, if not a necessary consequence, that the means and instrumentalities employed for carrying on the operations of their government, for preserving their existence, and fulfilling the high and responsible duties assigned to them in the Constitution, should be left free and un-

* Professor Powell points out that the doctrine of governmental immunity from taxation was generally, if not universally assumed long prior to the *McCulloch* case. *The Remnant of Tax Immunities*, 58 Harvard Law Review, at p. 787. See also cases cited in Cooley, on *Constitutional Limitations* (7 ed.) pp. 996-7, footnote 1.

> impaired, should not be liable to be crippled, much less defeated by the taxing power of another government, which power acknowledges no limits but the will of the legislative body imposing the tax."

As Judge COOLEY noted in *Constitutional Limitations* (2nd Ed.) p. [585]:

> "If the States possessed the authority to tax the agencies of the national government, they would hold within their hands a constitutional weapon which factious and disappointed parties would be able to wield with terrible effect when the policy of the national government did not accord with their views; while, on the other hand, if the national government possessed a corresponding power over the agencies of the State governments, there would not be wanting men who, in times of strong party excitement, would be willing and eager to resort to this power as a means of coercing the States in their legislation upon the subjects remaining under their control."

In *Pollock* vs. *Farmers Loan and Trust Co.*, 157 U. S. 429, 584 (1894), the rule was again reaffirmed in clear terms. Thus:

> "As the States cannot tax the powers, the operations or the property of the United States, nor the means which they employ to carry their powers into execution, so it has been held that the United States have no power under the Constitution to tax either the instrumentalities or the property of a State."

In *United States* v. *Railroad Company, supra*, this Court gave unqualified approval to the doctrine, saying (pp. 327-328):

> "The right of the States to administer their own affairs through their legislative, executive, and judicial departments, in their own manner through their own agencies, is conceded by the uniform decisions of this court and by the practice of the Federal government from its organization. This carries with it an

> exemption of those agencies and instruments, from the taxing power of the Federal government. If they may be taxed lightly, they may be taxed heavily; if justly, oppressively. Their operation may be impeded and may be destroyed, if any interference is permitted. Hence, the beginning of such taxation is not allowed on the one side, is not claimed on the other."

Chief Justice HUGHES in *Willcuts* v. *Bunn*, 282 U. S. 216, 224 (1930), characterized as a "familiar aphorism" the proposition stated in *Ambrosini* vs. *United States*, 187 U. S. 1, 7 (1902), "that as the means and instrumentalities employed by the General Government to carry into operation the powers granted to it are exempt from taxation by the States, so are those of the States exempt from taxation by the General Government."

After this fundamental principle had been continually acknowledged for almost a century, this Court, in *South Carolina* v. *U. S.*, 199 U. S. 437 (1905), departed from it and, for the first time, laid down a limitation upon the rule in so far as the immunity of states from federal taxation is concerned.

In *South Carolina* v. *United States*, the State adopted a law providing for a state monopoly of the sale of intoxicating liquor. Under the law, the State provided for the appointment of government agents to sell liquor at wholesale and retail in government-operated establishments. All proceeds of the operation of the establishments went to the State and the profits arising were divided between the State and its governmental subdivisions. A Federal statute provided that every establishment for the sale of liquor was required to be licensed and license tax fees were imposed upon such establishments by the Federal government.

The State, having paid the license tax charges for its establishments, sued in the Court of Claims to recover the

sums so paid, and upon the dismissal of its claim in that Court, appealed to the Supreme Court.

The Supreme Court (three of the Justices dissenting) affirmed the judgment of the Court of Claims.

This determination was founded upon the conclusion that the exemption of state agencies from Federal taxation applied only to those agencies which were "strictly governmental" in their nature, and did not extend to those activities of a state government which were, at the time of the adoption of the United States Constitution, those of an "ordinary private business" (pp. 461, 463). The Court reached its conclusion through reasoning which, we submit, does not stand up under analysis.

1. Proceeding by parity of reasoning from cases against municipalities arising in tort, Mr. Justice BREWER concluded that where a state agency engages in what is considered a "proprietary" activity, it loses its standing as a governmental instrumentality and becomes a private agency.

2. The only state agencies which were intended to be exempted from Federal taxation, said Mr. Justice BREWER, were those whose activities were regarded as "strictly governmental" at the time the Federal Constitution was adopted.

3. The tendency of the times, said Mr. Justice BREWER, was in the direction of state ownership of many hitherto private enterprises—a tendency which he seems to have regarded as destructive of the republican form of state government—and it was never contemplated that the state could, by such device, rob the Federal government of a very substantial part, if not all, its revenues. Mr. Justice BREWER seemed to be particularly impressed by the fact that the profits realized by the state from the operation of its liquor establishments were substantial, amounting to more than half a million dollars a year, and feared that "mingling the thought of profit with the necessity for regulation", states finding profit in such undertakings might en-

gage in them to the serious detriment of Federal tax revenues.*

The defects in the reasoning of the majority opinion are apparent upon mere inspection, as Mr. Justice WHITE, in his dissenting opinion, quickly demonstrated.

The suggestion that the State of South Carolina was, in its liquor-selling activities acting merely as a proprietor completely overlooked the fact that traffic in liquor is a common subject of state control because of the social consequences of its abuse. Moreover, and more important, to import into the field of taxation, where precision and definition are absolutely essential, the utter confusion prevailing in the field of tort in regard to the liability of municipalities for "proprietary" as distinguished from "governmental" activities, (see *Brush* v. *Commissioner*, 300 U. S. 352, 362, *et seq.* (1936); Borchard, *Government Liability in Tort*, 35 Yale Law Journal, 129, 229) could only serve to promote obscurity and uncertainty. To apply as a test for determining what state activities are immune from Federal taxation, the situation existing prior to 1787 would result in patent absurdity. *Home Building & Loan Assn.* v. *Blaisdell*, 290 U. S. 398, 442-3 (1933).

Almost every governmental activity has both a proprietary predecessor and a present day proprietary analogue. Indeed, the early history of this continent affords striking examples of this fact on a very broad scale in the charters of the Massachusetts Company, the Virginia Company, and the Hudson Bay Company. Those organizations,

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* It should be noted that at the time of the *South Carolina* case the Federal government did not have available to it the great sources of tax revenue made possible by the 16th Amendment in comparison with which tax revenues obtained from liquor sales sink to insignificance. The fears expressed by Mr. Justice BREWER in regard to the threat of the disappearance of Federal revenue sources seem, in the light of events, as groundless as his fears that municipal ownership of public utilities would result in the destruction of our republican form of government.

though proprietary in nature, were at the same time governmental in every sense of the term. Coming down to later Colonial times we find that police activities were originally performed by private watchmen and are even today performed by private detective agencies. Fire fighting was originally carried on by private volunteers and is aided even today by private salvage corporations supported by insurance companies. Although governmental water supply systems existed in the ancient world (See brief submitted by the City of New York in *Brush* v. *Commissioner, supra*), in this country private water companies preceded municipal water supply systems and many such companies still exist alongside municipal systems. The disposal of garbage has been, in some states, first governmental then proprietary then back again to governmental. The operation of ferry boat transportation services by the City of New York was a function granted to it by the Dongan Charter in 1686 and the Cornbury Charter in 1708, yet similar services have been and still are supplied by private companies (see *Benson* v. *The Mayor*, 10 Barb [N. Y.] 223 [1850]). The operation of piers and docks has long been a private endeavor in many places, yet New York City has had publicly owned docks and piers for more than two centuries and has during that time derived substantial revenues from wharfage (see *Benson* v. *The Mayor, supra; Radway* v. *Briggs*, 37 N. Y. 255 [1867]). Proprietary traction companies originally supplied transportation facilities to cities and, where they have not been displaced by municipal transportation systems in whole or in part, still operate alone or in concert with municipal systems. Private turnpike companies and canal companies originally provided roadways, toll bridges and canals, and except as they have been displaced by state, municipal, and national highways and bridges and by state and national waterways still continue to do so. Federal, state and municipal light and power systems in many communities have displaced or supplemented private utility companies. Federal and state agencies, supply needs formerly or concurrently

supplied by mortgage companies and insurance companies. Banking, which one might regard as a typically commercial enterprise, is and long has been performed by goverment instrumentalities. Indeed, we need not be reminded that it was the normal and usual commercial activities of the Bank of the United States which brought about *McCulloch* v. *Maryland, supra.* Many states and municipalities provide garbage disposal, housing, lodgings and airfields concurrently with private enterprises. Marketing agencies in one form or another have been supplied by state and federal instrumentalities for many years alongside proprietary agencies providing similar services. It is thus clear that the test of "usual", "normal", or "historical" function is in reality no test at all which can be precisely or even reasonably applied.

Neither is the fact that a state derives substantial revenue from its activities an appropriate determining factor in considering whether or not the rule of tax immunity applies. Mr. Justice WHITE, in his dissenting opinion, disposed of this contention in apt terms (p. 469):

> "The contention that because one government may have derived income from the exertion of its authority, therefore the other government has a right to do likewise, even if the agencies of the other government be thereby taxed, reduces itself to this: That the power to burden arises from the very condition which prevents the power from existing. If pushed to its logical conclusion, the far-reaching result of the proposition that wherever revenue is derived from an act by one government, therefore the other may burden the agent or instrumentality of the other may be readily illustrated. Take the National Government. If in the exercise of its ample authority to establish national banks a tax is imposed on such banks and a revenue derived, do the States thereby become entitled, without the consent of Congress, to tax banks? Take the Post Office Department. If by the carrying of the mails revenue is derived by the Government of the United States, are the States from that fact entitled to tax the instru-

mentalities employed by the Post-Office Department? Take the ocean transport service of the United States. If under given circumstances a charge is made for transportation, and hence a revenue is earned, may the States cripple that service by taxation?"

See also

Brush v. Commissioner, 300 U. S. 352 (1936).

Both adherents and opponents of reciprocal governmental tax immunity have criticized the *South Carolina* case and demonstrated its shortcomings (Julius Henry Cohen and Kenneth Dayton, *Federal Taxation of State Activities and State Taxation of Federal Activities*, 34 Yale Law Journal, 807-833; Alden L. Powell, *National Taxation of State Instrumentalities*, [Univ. of Illinois, 1936], Ch. V, and pp. 124, *et seq.*).

It is apparent from an examination of the cases since 1905 that this Court has recognized a conflict between the fundamental principle of state sovereignty and the views expressed in the *South Carolina* case. In an effort to resolve the conflict the Court has cast about for a theory which would preserve the principle of state sovereignty and at the same time permit federal taxation of some state activities. In describing the ambit of the field of state activities which is to be taxable by the federal government the Court has attempted to contrive various tests which would admit the principle of federal non-interference with state governmental affairs yet affirm the principle stated in the *South Carolina* case. This result cannot be achieved, because the two principles cannot exist together—they are mutually exclusive.

An examination of the various tests shows in each of them the seeds of a confusion and an illogic equal to that prevailing in the field of municipal tort liability to which we have adverted (*supra*, p. 8):

Shortly after the *South Carolina* case was decided, the Court, through an opinion of Mr. Justice WHITE in *Murray*

v. *Wilson Distilling Company*, 213 U. S. 151, 154 (1909), sought to limit the rule to the proposition that a state did not have power "to destroy a pre-existing right of taxation possessed by the Government of the United States".

In *Ohio* v. *Helvering*, 292 U. S. 360, (1934), the Federal Government sought to collect a federal license tax fee from the State of Ohio as a retail liquor dealer and a wholesale liquor dealer, the State having a liquor manufacturing and selling monopoly within its territory. The State, pointing to the *Murray* case, *supra*, argued that since the 18th Amendment had already deprived the Federal Government of the field of liquor vending as a source of tax revenue, the State when it entered that field upon the repeal of the 18th Amendment did not deprive the Federal Government of a "preëxisting right of taxation". This contention the Court rejected and, denying the claim of the State to immunity, held that it was bound by the decision in the *South Carolina* case, *supra*, saying (at p. 369):

> "If a state chooses to go into the business of buying and selling commodities, its right to do so may be conceded so far as the Federal Constitution is concerned; but the exercise of the right is not the performance of a *governmental function*, and must find its support in some authority apart from the police power. When a state enters the market place seeking customers it divests itself of its *quasi* sovereignty *pro tanto*, and takes on the character of a trader, so far, at least, as the taxing power of the federal government is concerned."

In *Helvering* v. *Powers*, 293 U. S. 214 (1934) a street railway and its properties were taken over by the State of Massachusetts to be operated publicly for a period of ten years, pursuant to an act of the Massachusetts Legislature and the consent of the company. Under the statute the railway was placed in charge of a Board of Trustees appointed by the Governor of the State with the advice and consent of the Council. The trustees were to be paid by the company; the stockholders of the company were to continue to receive dividends; and at the end of the term the property was to

revert back to private control. During the period of public operation the State and its municipalities were to provide funds to meet deficits arising out of the operation of the company. In these circumstances the Court held that the salaries of the trustees, although they claimed to be public officials, were subject to federal income tax. Chief Justice HUGHES, writing for the Court, based his conclusion upon the ground that the operation of a street railway, like the sale of liquor in the *South Carolina* case, *withdrew a field of taxation from the Federal Government;* was not a *"usual"* governmental activity, but a business enterprise and was, therefore, not immune from federal taxation.

It seems clear that, if it had so desired, the Court could have founded its conclusion in the *Powers* case upon the fact that the arrangements providing for state operation of the railway were in reality merely a statutory device for the endowment of the railway company by the State to the extent of the Company's deficits. However, instead of basing his conclusion upon that ground, Chief Justice HUGHES stated that, even if the State had taken over the company's equipment in its entirety, the State would, nevertheless, be subject to federal taxation upon the railway properties and operations.

In *U. S.* v. *California*, 297 U. S. 175 (1935), the question presented was whether a state owned railroad was subject to the Safety Appliances Act (45 U. S. C., Sections 2, 6). The Court held the State bound by the provisions of that Act in the operation of its railroad. The basis of the Court's determination was that the principle by which state instrumentalities are exempted from federal taxation do not apply by analogy as a limitation upon the federal government's power to regulate interstate commerce. However, in discussing the immunity of states from federal taxation, the Court, citing the *South Carolina* case and those which followed the theory of that case, said (p. 185):

> "Hence we look to the activities in which the states have *traditionally* engaged as marking the boundary of the restriction upon the federal taxing power."

In *Flint* v. *Stone Tracy Company*, 220 U. S. 107 (1910), this Court in considering whether two proprietary traction companies were subject to a corporation tax, discussed the general subject of the limitations placed upon state immunity from federal taxation by the *South Carolina* case. The Court said (p. 172):

> "It is no part of the *essential* governmental functions of a State to provide means of transportation, supply artificial light, water and the like. These objects are often accomplished through the medium of private corporations, and, though the public may derive a benefit from such operations, the companies carrying on such enterprises are, nevertheless, private companies, whose business is prosecuted for private emolument and advantage. For the purpose of taxation they stand upon the same footing as other private corporations upon which special franchises have been conferred."

Nevertheless, in *Brush* v. *Commissioner*, 300 U. S. 352 (1937), the Court concluded that an employe of a city water supply system was exempt from the federal income tax law upon the ground that the activities of such an instrumentality are governmental. Summing up the cases, Mr. Justice SUTHERLAND said (pp. 361-2):

> "The phrase 'governmental functions', as it here is used, has been qualified by this court in a variety of ways. Thus, in *South Carolina* v. *United States*, 199 U. S. 437, 461, it was suggested that the exemption of state agencies and instrumentalities from federal taxation was limited to those which were of a *strictly* governmental character, and did not extend to those used by the state in carrying on an ordinary private business. In *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 172, the immunity from taxation was related to the *essential* governmental functions of the state. In *Helvering* v. *Powers*, 293 U. S. 214, 225, we said that the state 'cannot withdraw sources of revenue from the federal taxing power by engaging in businesses which constitute a departure from *usual* governmental functions and to which, by reason of their

nature, the federal taxing power would normally extend.' And immunity is not established because the state has the power to engage in the business for what the state conceives to be the public benefit. *Idem.* In *United States* v. *California*, 297 U. S. 175, 185, the suggested limit of the federal taxing power was in respect of activities in which the states have *traditionally* engaged.

> "In the present case, upon the one side, stress is put upon the adjective 'essential', as used in the *Flint* v. *Stone Tracy* case, while, on the other side, it is contended that this qualifying adjective must be put aside in favor of what is thought to be the greater reach of the word 'usual', as employed in the *Powers* case. But these differences in phraseology, and the others just referred to, must not be too literally contradistinguished. In neither of the cases cited, was the adjective used as an exclusive or rigid delimitation. For present purposes, however, we shall inquire whether the activity here in question constitutes an essential governmental function within the proper meaning of that term; and in that view decide the case."

In *Helvering* v. *Gerhardt*, 304 U. S. 405 (1938), the Court in determining that the salary of an employe of the Port of New York Authority was not exempt from the federal income tax again stated through its majority opinion that the test of whether or not a state activity is immune from federal taxation depended in general upon whether the state activity sought to be taxed is "essential" to the preservation of the government.

In regard to this, Mr. Justice BLACK, in a concurring opinion, said (pp. 426-7):

> "Conceptions of 'essential governmental functions' vary with individual philosophies. Some believe that 'essential governmental functions' include ownership and operation of water plants, power and transportation systems, etc. Others deny that such ownership and operation could ever be 'essential governmental functions' on the ground that such functions 'could be carried on by private enterprise.' * * *

> There is not, and there cannot be, any unchanging line of demarcation between essential and non-essential governmental functions. Many governmental functions of today have at some time in the past been non-governmental. The genius of our government provides that, within the sphere of constitutional action, the people—acting not through the courts but through their elected legislative representatives—have the power to determine as conditions demand, what services and functions the public welfare requires."

In *Allen* v. *Regents*, 304 U. S. 439 (1938), the Regents of the University of Georgia were public officers appointed to administer and control the University. That institution is a State facility. The University conducted athletic contests for which the general public was charged admission fees. The Regents brought suit against the Federal Collector of Internal Revenue to enjoin him from enforcing the federal admission tax law against them. That law levied a tax upon admission tickets to exhibitions. The tax had been collected by the Regents, but withheld from the federal tax authorities. The Court held that the University was subject to the provisions of the statute. Although the Court might well have found the result reached by it by regarding the tax as a levy upon the person purchasing tickets and not a tax upon the state, Mr. Justice ROBERTS, writing the majority opinion, said (p. 451):

> "In the final analysis what we must decide is whether, by electing to support a government through the conduct of a business comparable in all essentials with those *usually* conducted by private owners, a State may *withdraw the business from the field of federal taxation.*"

Thus, the confusion occasioned by attempts to base tax exemption of state instrumentalities upon a determination of whether their activities are "proprietary" or "strictly governmental", "essentially governmental" "usual governmental" or "commercial" profit-making or non-profit

making, or whether, not being "normally" governmental, they tend to withdraw from the federal government an existing taxable enterprise or activity, is manifest from an examination of the decisions of this Court:

The test of "strictly governmental" activity as of 1787 (*South Carolina* v. *U. S., supra*), gave way to the test of whether the activity destroyed a "pre-existing right of taxation possessed by the Government of the United States" (*Murray* v. *Wilson Distilling Company, supra*). Such a test would obviously redound to the advantage of states engaged in an activity before that activity was taxed by the Federal Government over those states which did not enter the particular field until after the activity was taxed. Presently, that test was abandoned (*Ohio* v. *Helvering, supra*), and in its place the test again suggested was that used in tort cases against municipalities, i.e., taxability of a state enterprise to depend upon whether that activity was "proprietary" or "governmental" (*Flint* v. *Stone Tracy, supra*). Such a test threatened to import into the law of taxation all the confusion and absurdity that years of conflicting rules had accumulated in the law of municipal tort liability, and very soon that test, too, was abandoned (*Brush* v. *Commissioner, supra*). In the meantime, an alternative test was growing up in the opinions of the Court: that of whether the state activity under scrutiny was "essential" or "non-essential" to the support of government. (See *Helvering* v. *Gerhart, supra*). Such a test, too, must fail, since not only are the terms concededly inexact and indefinite (*Helvering* v. *Therrell*, 303 U. S. 218, 223 [1937]), but their judicial definition threatens to find analogies in the hopeless morass of the "proprietary" against "governmental" in the field of municipal tort law. Similarly the tests of "usual" governmental activity (*Powers* v. *Helvering, supra*) offered neither a guide nor a direction: what is "usual" for a government depends upon what the government of the particular state has done in the past.

What might be "usual" or "traditional" in one state might be unusual or novel in another; what might be "essen-

tially" governmental must depend upon who makes the test and when; what is "proprietary" might none-the-less be "usual", "essential" or "traditional", dependent upon the what, where and when of the activity under scrutiny. (See *supra* pp. 8-10). Yet clearly the Court does not intend to discriminate between states in regard to taxation.

It thus appears that the tests for determining state immunity from federal taxation exemplified by the *South Carolina* case and those which have followed it in principle are so confusing and lacking in precision as to make it impossible to predict with any fair degree of accuracy whether a state activity is to bear the burden of a federal tax. It is a patent truism that the basis of a tax must be readily recognizable and that exactitude in determining whether a tax is in fact to be imposed is a *sine qua non* of proper taxation. The detriment to states and their instrumentalities which arises from the confusion created by the doctrine of the *South Carolina* case is clear: States and their instrumentalities cannot foresee whether they are to be taxed upon a particular proposed activity. With taxation looming as a factor of major importance in the conduct of activities, a state and its instrumentalities should be in the position of being able to determine what activities it can engage in safely without being burdened by taxation. If federal taxation is to be imposed upon new activities of state instrumentalities, public ownership and operation of utilities, provision by a state of low cost housing for its residents, and many other services vital to the community would be discouraged if not rendered impossible, despite the fact that the provision of such facilities by the state is dictated by circumstances. (See Cohen and Dayton, *Federal Taxation of State Activities, supra*).

(2)

The difficulty which this Court has experienced in dealing with the principle expressed in the *South Carolina* case and the variations on that principle attempted in the

cases which have followed it (supra pp. 10-18) arises out of the circumstance that the cases are in direct conflict with a basic principle of our form of federal government: that the states are independent sovereignties within their proper sphere, and taxation of one sovereignty by another is destructive of the sovereignty of the one taxed. The Court has repeatedly declared its adherence to the principle that states and the federal government are sovereign within their Constitutional spheres, and immune, in general, from federal and state taxation, respectively. It has reiterated that the respective immunities of the governments are "reciprocal"; and has repeatedly stated that both immunities proceed from identical reasons. See *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 522 (1922); *Willcuts* v. *Bunn*, 282 U. S. 216, 224-5 (1931); *Burnet* v. *Jergins Trust*, 288 U. S. 508, 514 (1933). See also on the sovereignty of the States *Munn* v. *Illinois*, 94 U. S. 113 (1877); *Fifield* v. *Close*, 15 Mich. 505 (1867); *Ashton* v. *Cameron County*, 298 U. S. 513 (1936). It is indeed "a familiar aphorism" that it is just as important to protect states from federal encroachments upon their sovereignty as it is to protect the Federal government from the encroachment of the states upon its sovereignty. Yet, on the one hand this Court has time and again held that regardless of the nature of the transactions engaged in by the Federal government it is immune from state taxation (supra, p. 3) while on the other hand it has stated that the immunity of states from federal taxation depends upon the nature of the State's activity sought to be taxed (supra, pp. 6-16). It would seem too clear for discussion that the sovereignty of a state is far more interfered with by the taxation of one of its public utilities than the sovereignty of the Federal government would be interfered with by local taxation based in part upon the value of federal-owned machinery in the hands of a private contractor located on lands owned by such a person. Yet, applying the test of the *South Carolina* case to the former the State might be taxed by the Federal government, while the latter remains immune from state taxation. *United States* vs. *Allegheny County*, 322 U. S. 174 (1944).

Presumably, under the last cited case and others of similar import, if the Federal government were to enter the liquor dispensing business it would be immune from state taxation, despite the *South Carolina* case and notwithstanding that in so doing it withdrew from the states a source of revenue.

The suggestion made in some of the opinions that the "supremacy" clause of the Constitution places the two sovereignties' power to tax upon different levels (*Helvering* vs. *Gerhardt, supra; Graves* vs. *New York ex rel. O'Keefe*, 306 U. S. 466 [1938]) is adequately met in Petitioner's Brief on Reargument (pp. 33-4) and in the Brief of the States (pp. 7-9, 17). We need only point out here, as did Mr. Justice NELSON in *Collector* vs. *Day, supra*, that the supremacy clause applies only within the sphere of government delegated to the Federal Government and that sphere did not include the power to impinge upon State sovereignty through taxation. Within its own sphere a State is just as supreme as the Federal government is in its sphere.

The very existence of the theory of "supremacy" as a means by which the Federal government escapes state taxation upon activities identical with those which the Federal government taxes when engaged in by states, implies a recognition that state taxation upon Federal enterprises would seriously hamper Federal activities. Surely the converse of that proposition is true and States would be hampered just as seriously by Federal taxation. See *United States* vs. *Allegheny County, supra.*

Recognition of this basic illogic—to say nothing of unfairness*—is apparent in the attempts which this Court has made to expand the field of state tax immunity beyond the narrow limits laid down in the *South Carolina* case, in order to preserve a measure of state sovereignty, while at the same time endowing the Federal government with a

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*See Powell, *The Remnant of Tax Immunities*, 58 Harvard Law Review 757, at p. 804.

power to tax particular state activities (See pp. 14-15; *supra*). The two purposes, however, are mutually exclusive, since, as Chief Justice MARSHALL pointed out in the *McCulloch* case, the exercise of a power to tax a sovereignty is consistent only with the existence of a power to control that sovereignty. Despite some dissent (*Panhandle Oil Co.* v. *Knox*, 277 U. S. 218, 223 [1928]; *Graves* v. *New York, ex rel. O'Keefe, supra*, at p. 489) Marshall's picturesque phrase is still true: "The power to tax is the power to destroy". This the Court has often demonstrated. See, as an example, *Magnano Co.* v. *Hamilton*, 292 U. S. 40 (1933).

As long as the doctrine of the *South Carolina* case and the variations upon that doctrine offered in other cases are permitted to stand the difficulty will remain. Whether a state activity is or is not "governmental" or "essential" should in all logic depend upon whether the government of the State, acting under its own Constitution and statutes, determines that the activity is governmental or essential; *New York City Housing Authority* v. *Muller*, 270 N. Y. 333 (1936); *Puget Sound Power & Light Co.* vs. *Seattle*, 291 U. S. 619 (1934). See also dissenting opinion of Mr. Justice BRANDEIS in *New State Ice Co.* vs. *Liebmann*, 285 U. S. 262, 280 *et seq.* (1932) and concurring opinion of Mr. Justice BLACK in the *Gerhardt* case, *supra*.* Such a determination should not be left to the federal courts.

The underlying principle of reciprocal immunity from taxation enjoyed by the Federal government and the state governments is that the sovereignty of the governments must not be interfered with (*supra*, pp. 4-6). No argument is necessary to persuade this Court that the tax revenues of states cannot be subject to taxation by the Federal government. If they were, a direct interference with the

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* Indeed, such a suggestion is implicit in the statement of Mr. Justice MURPHY that any activity undertaken by the government is, for purposes of according tax immunity, "governmental." *Federal Land Bank* v. *Bismarck Co.*, 314 U. S. 95, 102 (1941).

states' sovereignty would occur. But taxes form only a portion of a state's revenue and the amount of such revenues is dependent upon both the needs of the state government and the availability to the state of other sources of revenue. The more sources of revenues apart from taxation which are available to state government, the less the state government is required to collect by taxation. If a state engages in activities which produce revenue, the amount required to be collected through the ordinary medium of taxation is proportionately reduced. Thus, when a state collects filing fees from litigants in its courts it is reducing the amount required to be obtained by taxation for the support of its judicial machinery. Similarly, if a state or one of its instrumentalities were to supply utility services to its residents without direct charge as they now supply education without direct charge, its tax collections would have to be increased, whereas if it supplied them at usual charges and those transactions resulted in gain to the state the state would be free to reduce its tax levies. Can it be said that in the one case the activity is "governmental" and in the other "proprietary"? Examples can be catalogued *ad infinitum*. To do so, however, would not change the obvious fact.

Thus, whether Federal taxation be imposed upon strictly governmental activities or imposed only upon the so-called proprietary activities engaged in by the states and their instrumentalities, the sovereignty of the states is directly impinged upon by the federal government. The difference between taxing the receipt of state taxes and taxing other revenues of the states and their instrumentalities is purely one of degree and amount and not one of principle.

The fundamental principle of our form of government is that the states are, except as otherwise expressly provided in the Constitution, separate sovereignties beyond the control of the Federal government (*supra*, pp. 4-6). If the Federal government is permitted to tax the states and their in-

strumentalities in any of their activities it would indirectly but nonetheless effectively control the kind of activities in which the states could engage. If, for example, the Federal government were to tax the gross receipts of a municipal transportation service, it might—no doubt would—render it impossible from a financial standpoint for the municipality to engage in such an activity (See testimony of Mayor LaGuardia in Hearings Before House Ways and Means Committee on Tax Exempt Securities, 76 Cong. 1st Sess. [1939], pp. 270 et seq.; see also testimony of Comptroller McGoldrick in *Commissioner* v. *Estate of Shamberg* and *Same* v. *Estate of White*, 323 U. S. 792 [1944] den. cert. 144 Fed. (2) 998, 1019 [C. C. A. 2, 1944]). Similarly, if this Court were to declare that municipally-owned services and utilities and the host of activities engaged in by municipal governments, apart from those which this Court has recognized to be strictly governmental, were subject to taxation, the right of the states and their instrumentalities to engage in such activities would be, in a very substantial measure, controlled or destroyed by the Federal government. New York City, as do other municipalities throughout the country, maintains numerous facilities which it deems "essential" to the proper conduct of life in a progressive community. Such facilities—water supply, surface and subway transit, public markets, wharves and piers, low cost housing, to name at random a few of many—are of vast importance to a great city. To authorize a Federal tax upon such activities would not merely burden the City—it would probably make their maintenance financially impossible. If such a result were not a direct interference with state sovereignty it is difficult to imagine what would be.

Factors identical with those above described have led this Court uniformly to exempt federal instrumentalities, regardless of their character, from state taxation. (See cases cited *supra*, pp. 3, 19-20.)

The inevitable conclusion is, to paraphrase the Chief Justice in his consideration of federal activities, "all ac-

tivities of [state] government * * * must stand on a parity with respect to their constitutional immunity from taxation" (*Graves* vs. *New York ex rel. O'Keefe,* 306 U. S. 466, 477 (1939)), and since federal activities of every nature are immune from state taxation, so all state activities, regardless of their nature, must be immune from federal taxation.

Since we have concluded that, under our form of government, it is beyond the power of Congress to tax *any* state property, activity or income, it necessarily follows that a "non-discriminatory" tax on such matters may not be laid by Congress. The subject of when a tax is "discriminatory" is too broad a question to discuss here. It is sufficient for us to point out that many taxes though doubtless discriminatory in operation have none-the-less been declared "non-discriminatory" in law. See *Rapid Transit Corp.* v. *New York,* 303 U. S. 573, 582 (1937). To give a single example, a tax upon the annual gross receipts of every class of corporation in excess of $750,000,000. might in law be "non-discriminatory", yet might operate upon few corporations other than the City of New York as a municipal corporation. The City of New York, with its annual expense budget of $875,000,000., might be crippled in its fiscal affairs and the entire balance of its governmental activities might be completely thrown out of gear by such a tax upon its revenues. Thus, in practice the mere fact that in form a tax laid upon state instrumentalities was "non-discriminatory" would offer no protection to the states at all. Moreover, as Petitioner has demonstrated (Brief on Reargument, pp. 5-14) discrimination has never been the test for determining governmental immunity from taxation.

Conclusion.

As we stated at the outset of this Brief, we have not addressed ourselves to the separate problem of whether or not Congress may constitutionally tax the individual recipients of state moneys, property or services. Such, in reality, is all this Court authorized in the *Allen* case, *supra*, when it held valid the imposition of an admission tax, to be paid by the spectator, upon attendance at a state-conducted football game.

Whatever devices Congress may contrive to tax property before it reaches the hands of a state (*Liggett & Meyers Co.* vs. *U. S.*, 299 U. S. 383 [1936]) or after it leaves the hands of a state (*Graves* v. *New York, ex rel. O'Keefe, supra*) should be separately considered as they arise in this Court.

The doctrine of sovereign immunity from taxation is fundamental in our form of constitutional government. The immunity of the States from federal taxation flows from the same basic principles as the Federal government's immunity from state taxation, and has been reiterated time and again by this Court. The Court should adhere to the rule of state immunity from federal taxation and should repudiate the unsound limitation placed upon it by the *South Carolina* case. That case, if it is to survive as precedent at all, should be limited in its application to its own facts and its doctrine should not extend to state activities other than the sale of liquor.

It is submitted that this Court should call a halt to the incursions upon state sovereignty which are bound to result unless the states receive from the Federal government the

same degree of immunity from taxes which the Federal government receives from the states.

December 1, 1945.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

No. 5.

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, *Petitioners*,

v.

UNITED STATES OF AMERICA.

BRIEF AMICUS CURIAE OF THE AMERICAN PUBLIC POWER ASSOCIATION.

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BRIEF AMICUS CURIAE OF THE AMERICAN POWER ASSOCIATION.

Introduction.

This brief *amicus curiae* is submitted on behalf of The American Public Power Association. This Association is a nonprofit service corporation, organized under the laws of the District of Columbia. Its membership includes, among others, the following power systems, owned and operated by states or their political subdivisions:

Consumers Public Power District, Columbus, Nebraska; Department of Public Utilities, Colorado Springs, Colorado; Light and Power Department, Hudson, Massachusetts; Imperial Irrigation District, Imperial, California; Board of Public Utilities, Jamestown, New York; Board of Public Utilities, Kansas City, Kansas; Electric Power and Water Board, Knoxville, Tennessee; Lower Colorado

River Authority, Austin, Texas; Department of Water and Power, Los Angeles, California; Board of Water and Electric Light Commissioners, Lansing, Michigan; Memphis Light, Gas and Water Division, Memphis, Tennessee; Department of Lighting, Seattle, Washington; Electrical Department, Springfield, Illinois; and Borough Electric Works, Wallingford, Connecticut.

Certain federally operated power systems also subscribe to the services of the Association, but the Association does not purport to speak for any federal project or power system in the submission of this brief.

On October 8, 1945, the Court notified counsel in this case that they were requested to address themselves in their briefs and on oral arguments to two questions; and it is to these questions that the present brief is directed, restricted to the relation of these questions to the properties, activities and revenues of the state and municipal power systems of the country. The exhaustive review of the authorities contained in the briefs of the State of New York and of the Attorneys General, *amici curiae*, with which we are in accord, need not be repeated here.

The basic rule, which has been stated many times by this Court, declares that "the instrumentalities, means and operations whereby the states exert the governmental powers belonging to them are . . . . exempt from taxation by the United States." *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, 575 (1929). In general see also, *Ohio* v. *Helvering*, 292 U. S. 360, 365 (1934); *South Carolina* v. *United States*, 199 U. S. 437, 461 (1905); *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 157, 158 (1910); *U. S.* v. *California*, 297 U. S. 175, 184 (1936); *University of Illinois* v. *United States*, 289 U. S. 48, 59 (1933); *Brush* v. *Commissioner of Internal Revenue*, 300 U. S. 352, 371, 372 (1937).

Question I.

"1. May Congress constitutionally include for taxation in a generally applicable taxing act any state property or activity or the income derived by the state from them, or any other source, so long as the tax does not discriminate against the state, or so long as the tax is not laid on the interest taxed, merely because it is that of a state—and if income of a private person from a like source may be constitutionally taxed?"

Congress has never asserted the power to tax income derived by a state or its political subdivisions from its service of electricity to its citizens, nor to tax the properties utilized for such service or the activities represented thereby. It is questionable whether Congress ever will assert such a power, in view of the uniform course of Federal legislation designed to promote, encourage and expand municipal power ownership, referred to later.

But, as to the constitutional question presented, we respectfully suggest that the answer should be in the negative if the property, income or activity relates to a public service rendered by the state to its citizens. That is to say, the state and its political subdivisions may themselves supply to their citizens water, electricity, police protection, fire protection, sanitation, harbors, and perform any other activity directly related to the public health, safety and welfare, and in so doing are exercising governmental functions. *Brush* v. *Commissioner of Internal Revenue*, 300 U. S. 352, 370, 371 (1937). All of these are manifestly public services, and are subject to the absolute control of the state, which may grant or prohibit exercise thereof by private persons. The state is not obliged to delegate these functions, nor on the other hand, do they lose their close relationship to the public health, safety and welfare because some states do delegate some or all of them. *Brush* v. *Commissioner of Internal Revenue*, 300 U. S. 352, 371, 372

(1937). They are functions which state governments must perform or cause to be performed, even at a loss, if society and hence the state are to continue to function. Where the state causes them to be performed under franchise, they are licensed private ventures into a governmental field. The private venturer gains no tax immunity by entering the domain of the state's function under its franchise, but the state loses none by occupying its domain in full and excluding the entrepreneur.

Question II.

> "2. To what extent may a state, by enlarging its property ownership or its activities, withdraw from the reach of Federal taxing power property and income which are normally subject to Federal taxation when owned or received by private persons? See *United States* v. *California*, 297 U. S. 175, 184, 185, and cases cited?"

We believe that the answer suggested to the first question applies to the second: that the decision by the state or its political subdivisions to furnish directly the services required for its citizens' health, safety and general welfare, and hence necessary to its own continued existence, is not an enlargement of its functions, but an occupation of fields inherently governmental, even though this occupation displaces private persons theretofore occupying them by leave and franchise of the state.

If, however, the state must show that it has "traditionally" occupied the field, as suggested in *United States* v. *California*, 297 U. S. 175, 184, 185, cited in the Court's question, the proof, as to local public ownership of power systems, is at hand.

Historically, local public power ownership has as long a lineage, and as distinguished an ancestry, as private ownership. The first central generating station in the United States, the New York-Pearl Street Steam Station, was

placed in operation September 4, 1882, and the first hydraulic generating plant was placed in operation at Appleton, Wisconsin, October 15, 1882. Both were financed by private capital, but by the end of the same year four municipally owned electric utilities were in operation. See Department of Commerce, Special Census Report on Central Electric Light and Power Stations, 1902. By 1900, 732 municipally owned systems had been established, including Lansing, Michigan 1892, Austin, Texas 1895, Tacoma, Washington 1893, Columbus, Ohio 1899. By 1944, state and municipal systems had over 5,000,000 kilowatts of installed capacity, out of a total of 50,524,000. Federal systems had an additional 5,000,000 kilowatts, bringing the generating capacity of publicly owned systems, both state and Federal, to nearly 20 percent of the total for the nation. These systems produced over 43,000,000,000 kilowatt hours of energy, divided 15,000,000,000 for state and local and 28,000,000,000 for Federal systems out of a total for the entire country of roughly 231,000,000,000 kilowatt hours. See January 20, 1945 issue of Electrical World, P. 89.

If tradition is the test, the unbroken line of Federal statutes giving preference to states and municipalities in the use of sites under Federal control and in utilization of power generated by Federal projects, is entitled to weight in proof of the long and proper presence of the states and their political subdivisions in this field. Public power ownership as a traditional and usual function of local government has been recognized by every Federal statute touching the subject. The municipal power systems have never been treated by Congress as interlopers in a Federal tax preserve, but as long-established occupants of their legitimate governmental field in the service of their citizens. See he Act of April 16, 1906, sec. 5 (34 Stat. 117, U. S. C. Title 43, sec. 522), giving "preference to municipal purposes" in disposition of surplus power on reclamation projects. This was the first Federal statute dealing with electric power generated on government projects. Cf. Reclamation Power

Act of February 24, 1911 (36 Stat. 930); Federal Water Power Act, (Act of June 10, 1920, c. 285, sec. 7, 41 Stat. 1067; U. S. C., Title 16, sec. 800); Boulder Canyon Project Act, (Act of December 21, 1928; 45 Stat. 1057, ch. 42, sec. 5 c; U. S. C. Title 43, ch. 12 A, Sec. 617 d (c)); Bonneville Project Act (Act of August 20, 1937, ch. 720, sec. 4, 50 Stat. 731, 16 U. S. C. 832); Tennessee Valley Authority Act (Act of May 18, 1933, c. 32, sec. 10, 48 Stat. 64; U. S. C. Title 16, sec. 831 i); Fort Peck Project Act (Act of May 18, 1938, ch. 250, sec. 4, 52 Stat. 403, 16 U. S. C. 833); The Reclamation Project Act of 1939 (Act of August 4, 1939, ch. 418, 53 Stat. 1187, sec. 9 c; 43 U. S. C. 485); Water Conservation and Utilization Act of 1940, (Act of October 14, 1940, 54 Stat. 1119, sec. 9, ch. 861); Flood Control Act of 1944 (Act of December 22, 1944, 58 Stat. 890, sec. 5, 16 U. S. C. 825s).

Conclusion.

The constitutional immunity of municipal power ownership is sustained under any standard heretofore suggested in the leading decisions of this Court, that is to say, whether the activity is required to be "strictly governmental in character" *South Carolina* v. *United States*, 199 U. S. 437, 461 (1905), "employed in carrying on the governmental operations of the state" *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 157 (1910), "usual governmental functions" *Helvering* v. *Powers*, 293 U. S. 214, 225 (1934), "activities in which the states have traditionally engaged" *United States* v. *California*, 297 U. S. 175, 185 (1936), or affording protec-

tion "to the continued existence of the state" *Helvering* v. *Gerhardt*, 304 U. S. 405, 421 (1938).

Washington, D. C., November 29, 1945.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

No. 5

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY,

Petitioners,

v.

UNITED STATES OF AMERICA.

BRIEF FOR THE STATES AS *AMICI CURIAE*

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BRIEF FOR THE STATES AS *AMICI CURIAE*

Statement

The questions propounded by the Court's order on October 8, 1945 in this case are clearly addressed to every State in the Union. They go to the foundation of our entire constitutional system. They involve the continued existence of the States as free and effective instrumentalities of local government.

Under our constitutional system, the guarantee that the States should forever continue to exist is the first premise of American government. Upon the Attorney General of each State falls the sworn duty of defending his State's sovereignty. When the Court propounded its questions on October 8th, the President of the National Association of Attorneys General, John M. Rankin of Iowa, therefore directed the preparation of a preliminary draft of this brief and its submission to the Attorney General of each State for

comment and criticism. The annual meeting of our association on November 27-29, 1945, afforded an opportunity for the submission and consideration of the comments of the individual Attorneys General. By a unanimous vote, the incoming President, Attorney General Greek L. Rice, was vested with full discretion to take appropriate action. Accordingly, the Association, acting through its incoming President, has joined in this brief with the individual Attorneys General whose names are subscribed hereto.

This brief is submitted by the several States pursuant to the permission granted by Rule 27(9) of the Rules of this Court. It is submitted in accordance with the Court's admonition to a claimant of immunity in *Willcuts* v. *Bunn*, 282 U. S. 216, 233 (1931), that "No state has ever appeared at the bar of this court to complain of this federal tax." See also STONE, *J.*, dissenting in *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, 582 (1931).

The questions posed by the Court's order of October 8, 1945 are these:

> "1. May Congress constitutionally include for taxation in a generally applicable taxing act any state property or activity or the income derived by the state from them or any other source, so long as the tax does not discriminate against the state, or so long as the tax is not laid on the interest taxed, merely because it is that of a state—and if income of a private person from a like source may be constitutionally taxed?
>
> "2. To what extent may a state, by enlarging its property ownership or its activities, withdraw from the reach of the federal taxing power property and income which are normally subject to federal taxation when owned or received by private persons. See *United States* v. *California*, 297 U. S. 175, 184, 185, and cases cited."

As the Court knows, the Attorneys General filed no brief upon the original argument of this case. We believed

the case fell squarely within the rule of *Brush* v. *Commissioner*, 300 U. S. 352 (1937), and we would not have presumed to burden the Court with arguments addressed to the fundamental constitutional principles involved. This brief is filed solely because of the Court's questions.

While these questions are broad indeed, we necessarily assume that it is the intention of the Court to confine its decision and opinion to the facts of the particular case at the Bar. We assume that far-reaching and fundamental constitutional issues of the breadth encompassed by the Court's questions will not be foreclosed by this Court at this time and in this case.

The States direct this brief solely to the Court's questions. We do not argue the merits of the specific controversy out of which the present case arises. We do not treat at all the extent to which private persons or corporations may enjoy derivative immunity. We consider only the question of direct taxes upon the States themselves and their property, activities or income. In this connection we, of course, mean "the States" to include their political subdivisions.

Our approach is guided by the breadth of the Court's questions. The questions invite not a review of precedents but rather an analysis of the basic policies involved in the field of intergovernmental immunities. They invite a review of our system of government that will be of assistance in adapting the road that has been followed in the past, and upon which the work and achievements of our States and Nation have proceeded, to the democratic problems of the present and of the future.

There is, of course, no conflict concerning the basic rule of state immunity from direct taxation. The Court has stood inflexibly upon this principle through all the ebb and flow of the conflicts on derivative immunity and on the nature of a "governmental function." It is the one rule on

which dissenting justices agree with majority justices, and reversing and overruling opinions agree with reversed and overruled opinions. With all the controversy in this field there has never been the faintest suggestion that the Congress could subject the States to taxation generally, merely because the taxes were non-discriminatory.

So it is not likely that the basic rule of immunity needs clarification, but rather the exception to the rule which has labored to distinguish between "governmental" and "non-governmental" functions. The questions propounded would seem to indicate the Court's dissatisfaction with the delineation of the character of these functions by "the gradual process of historical and judicial 'inclusion and exclusion' "[1]—a dissatisfaction that was foreshadowed by Mr. Justice BLACK in 1938[2] when he wrote critically of attempts to pass judgment upon the character and quality of various state activities, and to categorize them as "governmental" or "non-governmental" in accordance with what he called "individual philosophies" about the proper sphere of state activity.

Point I is addressed to the Court's first question. In it are considered arguments for and against federal power to tax all state property activities and income if the tax be non-discriminatory. We have chosen this approach to the issue as a matter of logical analysis, even though as a practical matter it would involve the complete disruption of practically all of the normal and established functions of state and local government and in many cases their utter bankruptcy. We assume that such a drastic change in our system of government will be approached, if at all, only by the orderly processes of constitutional amendment. If such an overthrow of the normal functioning of state and local government were ever attempted by judicial process, the people would be faced with the immediate necessity of

[1] *Brush* v. *Commissioner*, 300 U. S. 352, 365 (1937).
[2] *Helvering* v. *Gerhardt*, 304 U. S. 405, 424 (1938).

convening a constitutional convention to reconstruct the necessary divisions of general and local government and to repair the collapse of state and municipal finances that would instantly follow in the wake of such a decision. But even though the realities make it inconceivable that the Court would consider turning back the clock of constitutional interpretation through an orbit of one hundred and fifty years, a reappraisal of the unsoundness of such a policy, even as a matter of original consideration, would seem to be helpful.

We do not consider that there is any different limitation on federal taxation of state income than on state property or activities. The Sixteenth Amendment is subject to the same implications to protect the federal system as the rest of the Constitution. We do not discuss in this brief the discredited arguments that the Amendment enlarged the federal power to tax the States. If the Court is interested in our position on that question, the answer is provided in the brief which was submitted in 1939 to the Senate Finance Committee and the House Ways and Means Committee by the Attorneys General of thirty-nine States.[1] An excellent summary was provided in the Senate Subcommittee Report on the subject which was accepted by vote of the Senate, September 19, 1940.[2]

We would not be discharging our full obligation to this Court or to the country if we contented ourselves merely with a negative answer to the Court's first question. The problem of intergovernmental taxation and immunity would still remain for solution. Two approaches are possible in determining to what extent the basic rule of state immunity should be limited by other considerations: (1) the necessities of an effective federal government; or (2) the nature of the state activity.

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[1] Part III of "The Constitutional Immunity of State and Municipal Securities." Copies are on file in the library of this Court.

[2] 76th Cong., 3d Sess., Report No. 2140, Part 2, pp. 33-41.

Accordingly in Point II we shall appraise an interpretation of the Constitution which would permit federal taxation of the States only to the extent that such taxation is proven as a matter of fact to be necessary to the continued existence of the federal government. This is an interpretation of the Constitution which is, not only in accord with basic constitutional theory but is workable and would end the plague of recurring litigations in this Court. Our conclusion is that taxation of the States is certainly not necessary at the present time to maintain the federal government, and that it is highly improbable that the day will ever come when such necessity will exist.

In Point III we consider the alternative approach of the requirements for effective state government. Here we assume, for argument's sake, that the Court may prefer to retain the line between taxable and immune activities of the States in terms of the nature of the state function. If it is felt that any useful purpose is met by such distinctions, our analysis leads us to the following conclusion: that state immunity extends at least to those activities undertaken to promote the public welfare, health and safety even though they incidentally yield revenues.

Such an interpretation does not weaken the federal government and furnishes the States a much needed and adequate protection from federal interference. It is an interpretation which avoids putting a strait-jacket of federal taxation on the necessary activities of the States in a modern world. Freedom of local government to adapt itself to the changing necessities of the health, welfare and prosperity of its people is the very breath of our democracy. It is a rule which does no violence to precedent. It was the rule of the first Supreme Court case which considered the objection that a State's activity was not "governmental." *United States* v. *Baltimore & Ohio R. R. Co.*, 17 Wall. 322 (1873); it is the rule of the last two cases on the question:—*Brush* v. *Commissioner*, 300 U. S. 352 (1937);

Allen v. *Regents*, 304 U. S. 439 (1938). It does much to explain the cases of *South Carolina* v. *United States*, 199 U. S. 437 (1905), *Ohio* v. *Helvering*, 292 U. S. 360 (1934), and *Helvering* v. *Powers*, 293 U. S. 214 (1934). It is the only rule which is based on a difference in the nature of state functions and yet is consistent with the reasoning in the latest cases in the field of intergovernmental immunity, those regarding federal immunity. *Pittman* v. *Home Owners' Loan Corp.*, 308 U. S. 21 (1939); *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 98 (1941); *City of Cleveland* v. *United States*, 323 U. S. 329 (1945). It is, finally, a workable rule, easy to apply, not changing with changing philosophies of successive courts. It is a rule which would make it unnecessary for the Court to admit again that: "Looking backward it is easy to see that the line between the taxable and the immune has been drawn by an unsteady hand." *United States* v. *Allegheny County*, 322 U. S. 174, 176 (1944).

In Point IV we shall apply the conclusions reached in the first three Points to the specific questions asked by the Court. Our answers will be:

(1) Congress may not constitutionally include for taxation in a generally applicable taxing act any state property or activity or the income derived by the State from them or any other source, if no more is shown than (a) that the tax does not discriminate against the State or is not laid on the interest taxed merely because it is that of a State, and (b) that income of a private person from a like source may be constitutionally taxed. There is no present necessity for Congressional taxation of the States; on the other hand, the necessity for preserving the States as effective and functioning governmental units requires that immunity from federal taxation shall extend at a minimum to all activities undertaken by the States to promote the general welfare and to all property used therein and all income derived therefrom.

(2) A State may, by enlarging its property ownership or its activities, withdraw from the reach of the federal taxing power, property and income which are normally subject to federal taxation when owned or received by private persons, at the very least to the extent that the property is owned or the income derived in connection with an activity which the people of the State believe "should be rendered by the city (or State) itself as an appropriate means of discharging its duty to protect the health, safety and lives of its inhabitants." See *Brush* v. *Commissioner*, 300 U. S. 352, 371 (1937), and cases cited.

POINT I

A consideration of the proposition that intergovernmental taxation should be permitted if it is nondiscriminatory.

Let there be no mistake. A rule which would make discrimination the only test of the immunity of the States and the federal government from taxation by each other is not a test of immunity at all. It is the rejection of the doctrine of immunity. It would leave as the sole objection to taxation of a sovereign the same objection of discrimination which is available to any citizen of the sovereign. It would lower the government to the same plane as the private corporation. It would weaken the ties which have held the federal system together. It would not even have the virtue of ending a troublesome source of litigation between the States and the central government but would merely replace the old arguments with new questions as to what was a discriminatory tax and as to which classifications of the States and their agencies and their activities and their property are reasonable and which are unreasonable. See *Miller* v. *Milwaukee*, 272 U. S. 713 (1927); *Na-*

tional Life Ins. Co. v. *United States*, 277 U. S. 508 (1928); *Macallen Co.* v. *Massachusetts*, 279 U. S. 620 (1929); *Pacific Co.* v. *Johnson*, 285 U. S. 480, 493 (1932); *Schuylkill Trust Co.* v. *Pennsylvania*, 296 U. S. 113 (1935).

In introducing this point, we submit that it appears impossible to draft any income tax law which would not discriminate against the State, and would not tax the State's income because it is that of the State,—other than a law taxing all incomes alike at a single, flat rate without any exemptions or credits. Moreover, an attempt to do so would raise insuperable difficulties, due to the rule that to be constitutional, classifications for tax purposes must have a reasonable basis.

The considerations which validate the various classifications contained in the income tax provisions of the existing Internal Revenue Code from the constitutional standpoint are well known—those that justify taxing one individual at one rate and another at a higher rate or not at all, and that justify taxing corporations at different rates from either of them. They include ability to pay, the reasonableness of discriminating between large and small accumulations of *private* wealth, etc. These considerations have no application to the States.

Progressive tax rates involve taxing one State or City at a higher rate than another merely because its income is larger. Yet clearly to discriminate between States and Cities on the basis of the size of their income would be unconstitutional.

If we can conceive of federal income taxes on state and local tax receipts, it is apparent that the size of the tax receipts has no direct relation to ability to pay as in the case of private corporations. A metropolis like Detroit may be in dire straits with receipts in the millions of dollars while a small town may have much greater ability to pay percentagewise although its receipts are measured only

in thousands. Some tax formula would have to be evolved to meet the special circumstances of the State or municipality but then it appears that the ordinary provisions for the taxation of private corporations cannot apply. It is at once clear that there would immediately have to be a separate chapter in the Internal Revenue Code dealing exclusively with the taxation of the States and their agencies. Any conceivable federal program of taxing the income of the States would necessarily be leveled at the States because they are States.

The foregoing of course proceeds upon the assumption that an attempt is made to tax the revenues received from state and local taxation,—an assumption which may be implicit in the question whether Congress may tax "the income derived by the states * * * from any other source," although we are doubtful whether the Court intended such assumption to be made. The same result is reached however even if taxation of the tax receipts of the States and their agencies is not involved. In that case, presumably the attempt to tax would apply only to revenues of projects where charges are made. Here again, the application of any system of progressive income taxes to state and municipal revenues can have no reasonable basis.

Many unique problems are raised at once if the constitutional barriers against federal taxation of state and municipal income are let down.

An underlying and controlling factor is that each and every piece of state or municipal property and each and every dollar of state or municipal income belongs to the people of the States, being held in trust for them by the state or local government. In the case of a State, are all its subordinate agencies, incorporated or unincorporated, including its political subdivisions to be consolidated for the purpose of filing a single return, or is each state agency to be considered an independent undertaking for income

tax purposes? Should a City be required to file a single return reporting its income from pier rentals, airport rentals, water charges, bridge tolls, museum admissions, college tuitions and transit fares, or should each separate activity be considered a unit? A state activity which produces revenues may be only one part of a public project, the whole of which produces no surplus; is the revenue producing portion of the project to be isolated and a federal tax on its income required? Are the State and the City to be permitted to deduct from their normal and ordinary expenditures in carrying on state and municipal affairs? In the case of a State or City or Authority or Commission or District, is the cost of erecting a schoolhouse to be considered a capital improvement or a deductible operating expenditure? Is the repayment of public debt to be considered a proper deduction against gross revenues, in addition to the normal private deduction for interest only?

The suggestion that there may be federal taxation of the income of the States and their agencies is too new and revolutionary to permit appreciation of the enormous number of unique problems which it would occasion. But one thing is certain,—that it is impossible to think in terms of equal treatment of state and private income. For that reason, the condition inserted in the first question asked by the Court in this case cannot materialize. It is impossible for Congress to include state income in a generally applicable taxing act which "does not discriminate against the State" or "is not laid on the interest taxed merely because it is that of a State."

Wherever it has been argued that absence of discrimination removes all constitutional objections to a tax by one government of the agencies of the other, this Court has rejected or ignored the argument. *Dobbins* v. *Commissioners*, 16 Pet. 435 (1842); *Bank of Commerce* v. *New York City*, 2 Black 620 (1863); *Collector* v. *Day*, 11 Wall. 113 (1871); *Pollock* v. *Farmers Loan & Trust Co.*, 157 U. S.

429 (1895); *James* v. *Dravo Contracting Co.*, 302 U. S. 134 (1937); see also *Helvering* v. *Gerhardt*, 304 U. S. 405, 413 (1938).

I. Taxation of One Sovereign by Another Is Repugnant to the Concept of Sovereignty.

We shall first consider the doctrine of immunity apart from precedent, both as it squares with the philosophy of sovereignty and as a practical necessity for the preservation of our federal system. We shall then consider the actual effects on our federal system and on state finances should the Court, at this late date, strike down the established immunity under which the States and their political subdivisions have developed their local institutions and public activities.

Both the States and the federal government are sovereign. Indeed, the States, under the Tenth Amendment, are the ultimate repository of all sovereignty not delegated to the federal government, so that their sovereignty is in a sense fuller. Taxation is an exercise of sovereignty—it is not a process which normally acts *upon* the sovereign. There is normally no program of taxing sovereignties because there is normally only one sovereign in any given territory. But the genius of the American constitutional system is its concept of a federalism within which two coordinate sovereigns must coexist, each acting in the same territory.

Taxation of one government by another is demeaning to the sovereignty of the former. It implies a subordination of the taxed to the taxing government which does not exist in our American federal system.

Taxation is generally an exaction by or under the authority of the sovereign either solely to raise revenues for its support or also for regulatory purposes. But neither the

States nor the federal government are sovereign over the other. Neither has that authority over the other which is the essence of the power to tax.

Under the concepts of our federal system, only reciprocal immunity is sound unless there is to be reciprocal taxation *in toto*. We believe this because we believe in the supremacy of both the States and the federal government in their respective spheres. Arguments drawn from dicta that immunity should be a monopoly of the federal government because of its "supremacy" do not square either with accepted constitutional doctrine or good public policy. The supremacy of the central government in its sphere received formal recognition in the Constitution. The supremacy of the States in their sphere was just as formally recognized when it was reserved in the Tenth Amendment. Yet Chief Justice MARSHALL regarded both of these clauses as surplusage and said that the same result would have had to be implied anyway from the nature of the powers delegated and withheld. See *M'Culloch* v. *Maryland*, 4 Wheat. 316, 405, 406 (1819).

This is the reply to the suggestion that the federal power to tax is supreme over the States' power to perform their functions and that the federal government's power to perform its functions is supreme over the States' power to tax, so that only the federal government may claim immunity. The confusion in this suggestion is between the sphere of federal activities and the machinery by which the federal government may support itself. The power to regulate interstate and foreign commerce is part of the federal government's sphere in which it is supreme; its power to tax is mere machinery. The supremacy of the federal government is only in its special sphere—it does not attach to the taxing machinery.

This has been said in many Court opinions. For example, when the United States argued in 1871 against any reciprocal state immunity in *Collector* v. *Day* on the

ground that only the United States is supreme, this Court answered:[1]

> "The general government, and the states, although both exist within the same territorial limits, are separable and distinct sovereignties, acting separately and independently of each other, within their respective spheres. The former, in its appropriate sphere, is supreme; but the states within the limits of their powers not granted; or, in the language of the 10th Amendment, 'reserved,' are as independent of the general government as that government within its sphere is independent of the states. * * *
>
> "The supremacy of the general government, therefore, so much relied on in the argument of the counsel for the plaintiff in error, in respect to the question before us, cannot be maintained. The two governments are upon an equality * * *."

2. The Value of the Federal System.

No one can take issue with this Court's statement "that the preservation of the States, and the maintenance of their government, are as much within the design and care of the Constitution as the preservation of the Union and the maintenance of the national government. The Constitution, in all its provisions, looks to an indestructible Union, composed of indestructible states." *Texas* v. *White*, 7 Wall. 700, 725 (1869). The necessity of the States and the federal system of independent local government was very clear in the minds of the founders of the nation.

During the debates on the adoption of the Constitution in 1787, we find it recognized that

> "no extensive empire can be governed upon republican principles, * * * such a government will degen-

[1] 11 Wall. 113, 124, 126 (1871).

> erate to a despotism, unless it is made up of a confederacy of smaller states, each having the full power of internal regulation. This is precisely the principle which has hitherto preserved our freedom."[1]

a proposition which, incidentally, has been recognized in the organization of the United Nations.

Marshall said in 1819, "No political dreamer was ever wild enough to think of breaking down the lines which separate the states and compounding the American people into one common mass."[2]

Yet a generation later, in his farewell speech at Harrisburg, Andrew Jackson still felt it necessary to warn against the danger of the encroaching power of the federal government:[3]

> "It is well known that there have always been those amongst us who wish to enlarge the powers of the General Government; and experience would seem to indicate that there is a tendency on the part of this government to overstep the boundaries marked out for it by the Constitution. * * * There is but one safe rule, and that is, to confine the General Government rigidly within the sphere of its appropriate duties."

Through the years, the greatest Americans have felt the importance of the federal system keenly enough to warn against the destruction of the States. An outstanding statement is by Charles Evans Hughes:[4]

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[1] P. L. Ford—Pamphlets on the Constitution of the United States Published During Its Discussion by the People, 1787-1780.

[2] *M'Culloch* v. *Maryland*, 4 Wheat. 316, 403 (1819).

[3] Gen. Jackson's Farewell Address to the People of the United States together with his Proclamation to South Carolina, Harrisburg—Printer, J. M. G. Lescure, 1850.

[4] Report of New York State Bar Association, Volume XXXIX (1916), pp. 273-274. Italics supplied.

"But in the face of the difficulties already upon us, and destined to increase in number and gravity, we remain convinced of the necessity of autonomous local governments. An overcentralized government would break down of its own weight. It is almost impossible even now for Congress in well-nigh continuous session to keep up with its duties, and we can readily imagine what the future may have in store in legislative concerns. If there were centered in Washington a single source of authority from which proceeded all the governmental forces of the country—created and subject to change at its will—upon whose permission all legislative and administrative action depended throughout the length and breadth of the land, I think we should swiftly demand and set up a different system. *If we did not have States we should speedily have to create them.* We now have them, with the advantages of historic background, and in meeting the serious questions of local administration we at least have the advantage of ineradicable sentiment and cherished traditions. And we may well congratulate ourselves that the circumstances of the formation of a more perfect Union have given us neither a confederation of States, nor a single centralized government, but a Nation—and yet a Union of States each autonomous in its local concerns."

Woodrow Wilson said:[1]

"The development of the United States would have been as impossible without the state governments as the original establishment of our federal system would have been. They have furnished us with an ideal means of integrating a vast and various population, adapting law to changing and temporary conditions, modulating development, and permanently securing each item of progress."

He also said:[2]

"It would be fatal to our political vitality really to strip the States of their powers and transfer them to the federal government."

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[1] *Constitutional Government in the United States*, at page 50.
[2] *Id.* at p. 191.

Since free local government is the whole basis of democracy, it naturally had no existence under fascist domination in European countries. In Italy, the Fascist dictatorship, in its attack upon all things democratic, dispersed the locally elected municipal councils and set up in their place a municipal officer appointed by the central government.[1] In Germany the democratic Weimar Republic had given large measures of self-government to the cities. With these new found and, alas, short-lived freedoms, the German cities had greatly enlarged their municipal services, extended local suffrage, and might eventually have afforded the German people a primer in democracy of their own choosing. But this local self-government was one of the first victims of the Nazi hate for all things democratic.[2] And today, in trying to rebuild a democratic Germany which will not again imperil the whole world, our occupying forces are beginning with local self-government as the foundation.

Among our South American neighbors, weakness of local government goes hand in hand with recurrent dictatorships. Even Brazil, which originally had a federal form of government similar to ours, lapsed into dictatorship after the States had come under the control of Rio de Janiero. "Vargas struck at the entrenched rights of the separate states; * * * and abolished the independent state judiciaries; he is running Brazil with federally appointed interventors * * *."[3]

The lesson of our times bears out the warnings of Jackson, Wilson and Hughes: dictatorship destroys local self-government and works through centralized authority; and inversely, where local self-government is weakened and centralization advanced, the groundwork is laid for

[1] The Municipal Scene in 1939, by Prof. William Anderson, University of Minnesota, in the Municipal Year Book 1940, pp. 1, 2.

[2] *Ibid.*

[3] Inside Latin America, by John Gunther (1941).

dictatorship and the loss of democracy and human liberties. Thus, Franklin D. Roosevelt said:

> "We are safe from the danger (of oligarchy) just so long as home rule in the States is scrupulously preserved and fought for whenever it seems in danger."[1]

And again he said:[2]

> "* * * it was clear to the framers of our Constitution that the greatest possible liberty of self-government must be given to each State, and that any National Administration attempting to make all laws for the whole nation, such as was wholly practical in Great Britain, would inevitably result at some future time in a dissolution of the Union itself."

But preservation of American democracy is not the only issue in preserving our federal system. The whole world is groping today for a formula under which nations can unite for mutual self-protection without surrendering their sovereignty and local independence. We solved that problem in 1789 when we fashioned a federal system and made it work. That example is the greatest single contribution Americans can make toward the order of a postwar world. If our original thirteen nations could retain local independence and yet unite and forever ban war between them, the world can hope for an effective United Nations Organization. But it would be a mockery if the American States and local government should be under attack from within, at the very moment that the world turns to us as the exemplar of sovereign cooperation. Hopes for world cooperation would receive a sharp setback if our States should crumble, and new strength would be given to the argument that international cooperation should not be at-

[1] March 2, 1930.

[2] Quoted by the New York Times, September 17, 1937, p. 24.

tempted because it would end in the destruction of national self-determination in purely national concerns just as the States would be superseded in purely local concerns.

If we have labored the point that state independence must not be jeopardized, it is because no argument for state immunity can appeal unless there is a deep conviction that our federal system is worth retaining and that it is the bulwark of all our freedoms.

The reciprocal immunity rule was devised to protect that system. See *South Carolina* v. *United States*, 199 U. S. 437, 448 (1905); *Educational Films Corp.* v. *Ward*, 282 U. S. 379, 392 (1931); *Helvering* v. *Powers*, 293 U. S. 214, 225 (1934). It remains to show that it is necessary to the preservation of that system and the independence of the States.

3. Even as an Original Proposition, Immunity Would Be Necessary to Avoid Disruption of Our Federal System.

The rule of reciprocal immunities has always been considered a rule of necessity to preserve our federal system from actual destruction. It was in that real sense that *M'Culloch* v. *Maryland*[1] sought to preserve the federal government in the field in which it is supreme. And it was in the same sense that *Collector* v. *Day*[2] announced the immunity of the States in order to preserve their supremacy in their field. The rule is one of preservation of the federal system. It was to preserve the system that the immunity was applied first to the infant federal government when it needed protection from the ascendancy of the States; and it was for the same practical purpose that immunity was applied later to the States when they first required protection from a federal government whose security was established with the Civil War. The nec-

[1] 4 Wheat. 316 (1819).
[2] 11 Wall. 113 (1871).

essities of preserving the federal system apply equally to both state and federal governments in that system. No conceptual idea of federal supremacy in its sphere can restrict the logic of the rule to the federal government alone.

We shall not fall into the error of merely repeating Chief Justice MARSHALL's great pronouncement that "the power to tax involves the power to destroy." The phrase has been called a seductive cliché, yet its seductiveness lies in its fundamental truth when the opponents of the tax meet their obligation to explain wherein the challenged power to tax does in fact involve the power to destroy.

The way in which federal taxation would actually work toward the destruction of the States is not difficult to apprehend.

a. *Disruption by Regulation.*

Assume, for the moment, that the federal government had the power to tax the States by a non-discriminatory tax. The power to tax has always been held to contain the corollary power to make reasonable classifications of the objects to be taxed.[1] We assume, then, that the federal government would have the power to exempt certain state and local activities or property or income, while taxing all the rest. For example, the policy of the Treasury Department has for years been to secure taxation of the obligations of state and local governmental agencies generally—but not of local housing authorities. At some future time federal policy might favor activities which are self-liquidating as against activities which draw upon taxation for their support or vice versa.

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[1] *Brushaber* v. *Union Pacific R. R. Co.*, 240 U. S. 1, 24 (1916); see also *National Paper & Type Co.* v. *Bowers*, 266 U. S. 373 (1924); *Barclay & Co.* v. *Edwards*, 267 U. S. 442 (1924).

Taxation would, of course, discourage certain lines of state and municipal endeavor, while exemption would encourage other activities. The policy which would determine what local activities should be encouraged and what functions discouraged would not be local policy as it is at the present time, but a new and dominant federal policy. In other words, with the power to tax the States, the federal government would have a devastating power to substitute its idea of policy and propriety in purely local matters for the policy of the local governments. Local self-government would be so impaired as to be, in effect, destroyed. The syllogism is clear. The power to tax involves the power to exempt and the power to classify between taxable and exempt objects. The power to classify is the power to control and regulate. And once a sovereign is subject to the control and regulation of an outside sovereignty it is effectively destroyed; it ceases to act for itself and becomes a mere tool of the regulatory power.

For example, suppose that a federal government with power to tax all state activities, chose to exempt activities supported by taxes, but not activities supported by charges against the users. In the main, the revenues of these projects would not be sufficient to amortize the construction debt if heavy federal taxes were a charge on revenues ahead of amortization. Consequently, the economic pressure thus exerted would be to compel local abandonment of the policy of self-liquidating public enterprises. No State could be expected to resist the effort of the federal government to compel abandonment of self-liquidating enterprises if the alternative is to dip into tax receipts in order to support them. Yet, we submit, that the choice of such a policy in a purely local matter cannot, by the remotest stretch of the imagination, be considered as one proper for decision by the federal government.

The way in which the power to tax entails the power to regulate is illustrated by legislation now pending in

Congress. H. R. 2014 proposes to tax state and municipal revenue bonds used to finance the purchase of private utility systems by States or municipalities; otherwise it leaves the statutory exemption of state and political subdivision bonds undisturbed. From the announcement accompanying the introduction of the legislation, it appears that the objection is not to immunity of public obligations generally, but rather to the public purchase of private utilities by the use of revenue bonds. Investigation disclosed that the author of the bill objected specifically to the purchase of the Nebraska Power Company by an agency acting for the City of Omaha, the purchase being from the American Power and Light Company, a utility holding company under order of dissolution pursuant to the Public Utility Holding Company Act of 1935.

The suggestion soon appeared in another guise in hearings before a subcommittee of the House Committee on Interstate and Foreign Commerce charged with investigating the effects of the Public Utilities Holding Company Act. The chairman of the subcommittee took up the charge and specifically referred to the same public purchase of the Nebraska Power Company on behalf of the City of Omaha. The objection seems to be to payments made for the local utility properties which, in the opinion of the chairman, were excessive.[1] The use of this particular type of obligation was labelled "primarily for tax evasion."

Yet, as a matter of fact, this particular purchase of utility properties in Nebraska followed several years of public discussion and a special investigation by a committee of the Nebraska State Legislature.[2] The transaction was made possible by specific legislation of the State. Legis-

[1] New York Times, July 7, 1945.

[2] Final Report of the Nebraska Legislative Council, Sub-Committee on Public Power, dated September 27, 1944.

lature.[1] It was an issue of substantial prominence in the political and public life of Omaha for several years[2] and it was resolved in accordance with the decision of the representatives of the people in the city and state governments.

It would seem that the question of whether the City should purchase the property at all, the price to be paid and the method of financing the purchase were all matters for purely local decision. Yet, it has occasioned introduction of federal legislation intended to make such transactions impossible by carving out an exception to the general exemption of state and municipal obligations. The pendency of this legislation and the discussion of the merits of the local transaction in Congress at this time illustrate the way in which the power to tax state and municipal obligations, coupled with the power of selective exemption, would permit the federal government to substitute federal policy for local policy in purely local fields and to embark upon a regulation of local affairs of a type which would destroy the independence of the States. It shows more. It shows that if the power existed, there would be a will to exercise it.

Similarly, the federal policy might oppose solution of regional problems by interstate compact rather than through direct federal action. Such a policy might prompt taxation of joint state activities while exempting individual state action.[3]

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[1] LB-204 enacted at the 56th Session of the Nebraska Legislature, and approved by the Governor on May 26, 1943; additional legislation was adopted May 7, 1945 and was approved by the Governor on May 8, 1945.

[2] See Omaha Sunday World-Herald, Dec. 31, 1944; Omaha Morning World-Herald, January 1, 1945; Report of the Civic Committee on Power, published in Omaha Sunday World-Herald, February 18, 1945.

[3] The United States Attorney General argued for such a classification in *Commissioner* v. *Estate of Shamberg*, 144 F. (2d) 998 (1944), cert. den. 89 L. ed. Adv. Ops. 282 (1945).

Even with their present immunity the States are often without adequate resources to enable them to discharge their full duty to provide for the welfare of their people. Congress has recognized this fact and has tried by grants-in-aid to increase the resources of the States.[1] While such grants may help the economic situation of the States, they certainly weaken their independence and subject them to a great measure of federal control. If the States were to become taxable, the grants by the federal government would probably have to increase. The power to tax the States, therefore, would add little net gain to the resources of the federal government but would greatly increase the measure of federal control over the States' activities in the purely local sphere. This is borne out in the history of conditions annexed to the grants by the Public Works Administration and by the minute supervision of local governments in all their expenditures of the monies granted by the federal government.

Even the most "reasonable" classification, which could not at all be classed as "discriminatory" in a constitutional sense, would subject the States to pressures and controls which would destroy their independence.

b. *Disruption by Curtailment of Ability to Provide Services.*

Disruption, however, would come not from regulation alone. Atrophy through lack of funds to perform essential activities would be equally destructive of state government as it was to the central government under the Articles of Confederation. For example, suppose that a community wanted to organize an irrigation district, but the project was marginal in the sense that the anticipated cost of operation and amortization was close to the estimated maximum income. The project might be successfully accomplished if the added burden of federal taxation was not

[1] See Congressional Record, Oct. 22, 1945, p. 4766.

thrust upon the local government. A tax on the bonds to be issued would increase interest costs, and a tax on the operating surplus needed to amortize the cost of the project would make it impractical. The result would be that a service earnestly desired by the people of the locality would be destroyed before conception, by the mere federal power to tax. The result would be that a service would be foregone and the federal government would not even have the consolation of collecting the tax.

If the federal government could tax the properties and activities of the States the burden of that taxation would have to result either in increased federal grants or in the decrease of state activities or in an effort to increase the States' revenues to meet the added cost. Probably all would be attempted. The limited ability of the States to increase their revenues to meet the cost of a federal exaction, we shall treat below. But there would, inevitably, be a decrease in the quantum and quality of the public service which the States and Cities could continue to render if they were saddled with a great added burden of millions of dollars a year in federal taxes. And because local government in democratic America does not exist for itself, but only to provide for the welfare of its people, we may truly say that such an effect of the tax would be at least partial destruction of state government.

The same problem involves an even greater danger. The curtailment of local functions because of federal taxes would not be the end of the matter. It is not likely that these services, really desired by the people, would be readily surrendered. A vacuum is as abhorrent to the laws of political science as to the laws of physical science. Inevitably, there would be a strong tendency for the federal government, the recipient of the money of which the States would have been deprived, to move in and take over the functions which the local governments were forced to give up. While the States do not seek a competitive advantage

over private business, they must not be placed in the field of government itself at a competitive disadvantage with the federal government. The federal government may either tax itself or exempt itself; it makes no difference, because the taxing and the taxed pockets are the same, so that, in effect, the federal government is always exempt from its own taxation. If the States are taxed and the federal government thus, of necessity, continues exempt, the economic ability of the federal government to expand its activities at the expense of the States would create an irresistible trend toward ever greater centralization with all its inevitable evils in governmental and human values.

We cannot conceive that a Constitution which presupposes the continued existence of both state and federal governments as effective instruments of government, with powers in delicate balance, can be said to countenance taxation which can only result in a dislocation of the federal system and a vast enhancement of the federal sphere at the expense of the States. These are the arguments which have induced this Court in a score of cases to deny the federal government the power to tax the States, even though the tax is labelled non-discriminatory.

4. State Representation in Congress Is No Substitute for a Constitutional Guarantee of Immunity.

Of course what the Constitution forbids, Congress cannot do, even though it consists of the representatives of the people of the States. The essence of constitutional government as distinguished from parliamentary government is that there is a greater limit on the authority of the representatives in the Legislature than their own idea of the best interests of their constituents. This Court has always insisted that the acts of the people's representatives in Congress, no matter how well intentioned, are subordinate to the Constitution which is the highest law of all. It is, therefore, strange to find a hint in recent

dicta that where the protection of the independence of the States and the integrity of the Tenth Amendment are involved, a different philosophy may exist. See *Helvering* v. *Gerhardt*, 304 U. S. 405, 412 (1938). It is one thing to argue, as Marshall did in *M'Culloch* v. *Maryland*, 4 Wheat. 316, 435, 436 (1819), that the lack of federal representation in State Legislatures is a reason to forbid the States' taxation of federal institutions. It is a complete *non sequitur* to conclude that representation in Congress is a complete answer to Congressional action challenged as unconstitutional.

One of the prime purposes of a constitution in a democracy like ours was to protect certain fundamental rights of minorities from interference by the representatives of the majorities. When a citizen has complained that his rights of free worship, free speech, free assembly, are abridged by Congressional action, it has never been an answer that his representatives in Congress have adopted the legislation. We can imagine no theory more abhorrent to the constant American effort to safeguard human liberties. If our view is sound, it exposes the fallacy of answering the question of state immunity in terms of representation of the people of the States in Congress.

In a country as tremendous and diverse as ours, the interests of the States are rarely identical—over many issues they fall into majority and minority groups just as their people do. The representatives of a majority of States can outvote the representatives of the minority. The representatives of no single State have the veto power in Congress. Twenty-one coastal States have peculiar problems not common to twenty-seven inland States. The arid land States have common interests not shared by the New England States. Predominantly industrial States may not appreciate the problems of agricultural States. But standing above all this clash of interest is the Constitution which seeks to keep the balance between state and federal governments outside the field of legislative controversy.

The argument that since the States are represented in Congress they are capable of protecting themselves, begs the whole question of constitutionality. The dubious protection of a majority in Congress is no substitute for the rights guaranteed to the States by the Constitution itself. The whole principle of constitutionalism is that those rights are inviolable, Congressional majority or no Congressional majority. The suggestion that the sovereign position of the States must find its only protection in the will of a transient majority of Congress is a negation of the entire federal system.[1]

There is another great fallacy in suggesting that representation is adequate protection of the States from federal destruction. The plain fact is that since the adoption of the Seventeenth Amendment, the state governments, as such, are no longer represented in Congress. The Congressman or Senator is a part of the federal government and not of the state government. There is nothing in the nature of his office which prevents him from feeling that those people would be better served if the national government of which he is a part, should dominate the state government of which he is not a part.

The argument that the States must rely for their protection only upon their representation in Congress smacks of the old "confidence" theory. It asks each State to place its trust not in the Constitution, as expounded by this Court, but in its representatives and the representatives of other States in the federal Congress. The answer might well be:[2]

> "But is this a case of confidence? Would the people of any one State trust those of another with

[1] See "Views of the Minority of the Special Committee on Taxation of Governmental Securities and Salaries, created by S. Res. 303 (75th Congress)," 76th Congress, 3rd Session, Report No. 2140, Part 2, p. 31.

[2] *M'Culloch* v. *Maryland*, 4 Wheat. 316, 431 (1819).

> the power to control the most insignificant operations of their state government? We know they would not. Why, then, should we suppose that the people of any one State should be willing to trust those of another with a power to control the operations of a government to which they have confided the most important and valuable interests?"

How dangerous it is to rely solely on "confidence" in representation is shown by the recent history of the Australian States. The process began with a decision in 1920 weakening the doctrine of reciprocal immunities.[1] It ended with the destruction of the States in 1942 in *South Australia* v. *The Commonwealth*, 68 C. L. R. 373. That case upheld the constitutionality of four Commonwealth Acts which stripped the States of the power to levy income taxes and substituted a system of direct subsidies to compensate for the loss of revenues. To make assurance doubly sure the Commonwealth took over all state officers engaged in income tax assessment or collection and all equipment of the States for such administration. The statutes were bitterly attacked by all the Australian States as a deliberate scheme to preclude the States from securing the necessary revenues to function as States. The Court admitted the "scheme," saying, "The legislation which is attacked is not colourable —it admits its character upon its face." To the charge that state sovereignty was destroyed the Court said (65 C. L. R 373, 421):

> "It is unnecessary in the present case—and probably unnecessary in any purely legal controversy—to consider in what sense a State which is part of a Federal Commonwealth under the British Crown, can be said to be a 'sovereign state.'"

This decision was recognized in Australia as the end of their federal system and the sovereignty of their States.

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[1] *Amalgamated Society of Engineers* v. *Adelaide Steamship Co., Ltd.*, 28 C. L. R. 147 (1920).

The New York Times of July 26, 1942 carried the following dispatch from Canberra, Australia:

> "By Federalists and Unificationists alike the High Court's judgment validating a uniform income tax for Australia is regarded here as a landmark in constitutional history.
>
> "Former Prime Minister Robert Gordon Manzies, who doubted the validity of the legislation while approving its objective, declared it marked the end of the federal era in the constitutional relations of commonwealth states and the beginning of a new era in which the Government of Australia must be regarded as much more a unitary government and much less a federal system than it was previously thought to be. * * *
>
> "The unificationists consequently welcome the judgment as a first step toward great constitutional changes that will rapidly reduce the States to a subordinate position resembling that of the Provinces of South Africa."

According to another report from Canberra:[1]

> "it has been said that the taxation power now given to the Federal Treasurer is so great that he is just as much in control of the States as if his nominees were Premiers in each of them.
>
> "Moreover the High Court emphasized the paramount position of the Federal Government when the Chief Justice declared the Commonwealth could end the political independence of the States and this could not be prevented by any legal decision."

Australia is a warning to us of the necessity of constitutional protection of the States beyond any safeguards they receive from their representation in Congress.

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[1] The Christian Science Monitor, Boston, July 31, 1942, p. 5.

5. The Place of Precedent.

The basic immunity of the States even from non-discriminatory federal taxation has often been asserted and never questioned by this Court. The rule was not called into play regarding the States until the first federal act which might have been construed to tax state instruments (Stamp Act of June 30, 1864). The power of Congress to impose such taxes was immediately challenged in the State Courts beginning in 1864, and state immunity was unanimously upheld by the highest Courts of eleven States.[1] A dictum of this Court in *Veazie Bank* v. *Fenno*, 8 Wall. 533, 547 (1869) expressed this Court's agreement with the doctrine of state immunity. The opinion says:

> "It may be admitted that the reserved rights of the States, such as the right to pass laws, to give effect to laws through executive action, to administer justice through the courts, and to employ all necessary agencies for legitimate purposes of State Government, are not proper subjects of the taxing power of Congress."

From that day to this, this Court has unequivocally upheld the doctrine of state immunity in dozens of opinions: *Collector* v. *Day*, 11 Wall. 113 (1871); *United States* v. *Baltimore & Ohio R. R. Co.*, 17 Wall. 322, 327 (1873); *Railroad Co.* v. *Peniston*, 18 Wall. 5, 30 (1873); *Mercantile Bank* v. *New York*, 121 U. S. 138, 162 (1887); *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429, 584, 601, 652, 653; 158 U. S. 601, 630, 666, 693 (1895); *Plummer* v. *Coler*, 178 U. S.

Smith v. *Short*, 40 Ala. 385 (1867); *Bumpass* v. *Taggart*, 26 Ark. 398 (1870); *Duffy* v. *Hobson*, 40 Cal. 240 (1870); *State of Georgia* v. *Atkins*, 35 Ga. 315 (1866); *Latham* v. *Smith*, 45 Ill. 29 (1867); *Griffin* v. *Ranney*, 35 Conn. 239 (1868); *Warren* v. *Paul*, 22 Ind. 276 (1864); *State* v. *Garton*, 32 Ind. 1 (1869); *Eifield* v. *Close*, 15 Mich. 505 (1867); *Clemens* v. *Conrad*, 19 Mich. 170 (1869); *Davis* v. *Richardson*, 45 Miss. 499 (1871); *Haight* v. *Grist*, 64 N. C. 739 (1870); *Jones* v. *Keep*, 19 Wisc. 390 (*369) (1865); *Sayles* v. *Davis*, 22 Wisc. 217 (*255) (1867).

115, 117, 118 (1900); *Ambrosini* v. *United States*, 187 U. S. 1, 7 (1902); *Snyder* v. *Bettman*, 190 U. S. 249, 253-254 (1903); *South Carolina* v. *United States*, 199 U. S. 437, 452-454, 465 (1905); *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 147 (1911); *Farmers & M. Savings Bank* v. *Minnesota*, 232 U. S. 516, 526, 527 (1914); *Evans* v. *Gore*, 253 U. S. 245 (1920); *Metcalf* v. *Mitchell*, 269 U. S. 514, 521-523 (1926); *National Life Ins. Co.* v. *United States*, 277 U. S. 508, 521 (1928); *Willcuts* v. *Bunn*, 282 U. S. 216, 224, 225 (1931); *Educational Films Corp.* v. *Ward*, 282 U. S. 379, 389 (1931); *Group No. 1 Oil Corp.* v. *Bass*, 283 U. S. 279, 282 (1931); *Susquehanna Power Co.* v. *State Tax Commission*, 283 U. S. 291, 294 (1931); *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, 575, 579, 580 (1931); *Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393, 399, 400, 411 (1932); *Fox Film Corp.* v. *Doyal*, 286 U. S. 123, 128 (1932); *Burnet* v. *A. T. Jergins Trust*, 288 U. S. 508, 513, 514 (1933); *Trinityfarm Construction Co.* v. *Grosjean*, 291 U. S. 466, 471 (1934); *Helvering* v. *Powers*, 293 U. S. 214, 224, 225 (1934); *United States* v. *California*, 297 U. S. 175, 184 (1936); *Ashton* v. *Cameron County Water District No. 1*, 298 U. S. 513, 528-531 (1936); *New York ex rel. Cohn* v. *Graves*, 300 U. S. 308, 315 (1937); *Brush* v. *Commissioner*, 300 U. S. 352, 360, 374, 375 (1937); *Hale* v. *State Board*, 302 U. S. 95, 107, 109 (1937); *James* v. *Dravo Contracting Co.*, 302 U. S. 134, 152, 153, 157 (1937); *Helvering* v. *Therrell*, 303 U. S. 218, 223 (1938); *United States* v. *Bekins*, 304 U. S. 27, 52, 53 (1938); *Helvering* v. *Gerhardt*, 304 U. S. 405, 415 (1938); and *Allen* v. *Regents*, 304 U. S. 439, 453, 457 (1938).

Our own view of the importance of precedent in our judicial system is drawn from Mr. Justice CARDOZO's philosophy, in his "Nature of the Judicial Process:"[1]

> "I think adherence to precedents should be the rule and not the exception."

[1] Page 149. See also Report of New York State Bar Association, Vol. LV (1932), p. 271.

He stated the limited field in which the exception operates:[1]

> "I think that when a rule, after it has been duly tested by experience, has been found to be inconsistent with the sense of justice or with the social welfare, there should be less hesitation in frank avowal and full abandonment.
>
> * * *
>
> "If judges have woefully misinterpreted the *mores* of their day, or if the *mores* of their day are no longer those of ours, they ought not to tie, in helpless submission, the hands of their successors."

In the field of reciprocal intergovernmental immunities the arguments for the rule control, and those for the exception do not. None of the reasons for reversal which are suggested by Mr. Justice CARDOZO apply in this case; many sound arguments against it would exist in addition to the arguments we have already given. We are not in a field of sociology and changing *mores*. There is no question of injustice to private individuals because of an unfair exemption of public salaries.[2] Here the question is whether certain activities are to be exercised at all or by the federal government instead of by the States; and whether the federal government shall gather revenues by taxation of the States or the States shall be left free to devote those sums to local government, according to their own policies. It is a choice between free and regulated local government.

This is a great question of the form of our federal system and the balance of powers within that system. There is no change in the need for that balance. The lesson of rampant centralization and dictatorship in other lands points rather in the direction of a greater need today for

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[1] *Id.* at pp. 150, 152.

[2] *Cf. Helvering* v. *Gerhardt*, 304 U. S. 405 (1938).

the protection of our States than when the rule was first fashioned. The form of our government is too fundamental a concern for such changes to be undertaken judicially rather than by constitutional amendment.

We shall show more fully in Point II that no change in precedent is necessary to avoid a threat to the revenues of the federal government. The federal government has never collected revenues from the States, except small excise and license taxes in connection with the sale of spiritous liquor[1] and from taxes on admissions to amusements furnished by the State.[2] None of the host of other activities of state government have yielded any revenues to the federal treasury. Yet in a time of federal need which will probably never be surpassed, the federal government was able, in the last few years, to raise unprecedented billions of dollars of revenues to support itself and was able to carry on with practically no contribution from taxation of the States, their public projects and their statewide and municipal activities. For the past forty or fifty years the States and their agencies have been operating water systems, toll bridges, local utility systems, ferries, municipal transit systems and various local utilities without paying federal taxes thereon. It is in such a setting and with such a background of state and local custom and practice that the federal government was able to increase its tax revenues from $1,891,290,000 in 1932 to $7,818,365,000 in 1941[3] and to $46,456,554,000 in 1945.[4] In the light of such federal re-

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[1] See *South Carolina* v. *United States*, 199 U. S. 437 (1905); *Ohio* v. *Helvering*, 292 U. S. 360 (1934).

[2] *Allen* v. *Regents*, 304 U. S. 439 (1938). Whether this was a tax on the State or on the patrons was not decided; it was only decided that in either event the tax was valid.

[3] U. S. Dept. of Commerce, Bureau of the Census, State and Local Government Special Study No. 20, "Financing Federal, State and Local Governments: 1941" (Sept. 1942), Table 9.

[4] Gross revenues were $47,739,524,339; payment into the Old Age and Social Insurance Trust Fund was $1,282,969,759. Daily Statement of the Treasury Department, June 30, 1945.

sources the usual argument that state or local activities are endangering the ability of the federal government to carry on its functions, becomes utterly ridiculous.

In the face of this fact, we cannot see that the immunity of the state governments has ever threatened the destruction of the federal government by withdrawing vital sources of federal revenues.

6. Reversal of Precedents at This Time to Permit Taxation of All State Activities Would Disrupt State Fiscal Systems Established on the Basis of the Law as It Stands.

Although it is enough to support an established doctrine that there is no sound reason to change it, the States can list many compelling reasons against such a change.

Despite the breadth of the first question propounded by the Court, we necessarily assume that the Court did not intend to suggest the possibility of federal taxation of tax revenues received by the state and municipal governments. The effect upon state and municipal fiscal affairs of such a tax is obvious. Accordingly, the consequences of federal taxation as they are considered in the ensuing portions of this brief are confined to the chaos in state and municipal finances that would be brought about by any declaration by this Court that the federal government had the power to tax state and municipal activities, property and income other than tax revenues.

If the doctrine of intergovernmental immunity had not been established as part of the very fabric of our federal system, the relations between the federal and state governments would have proceeded on a very different course from that recorded in the history of the past 150 years.[1] The power to tax incomes without apportionment might not have been ratified by the States in its present form.

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[1] See cases cited pp. 31-32, *supra*.

The debates in Congress and in the State Legislatures at the time of its adoption demonstrate that very clearly.[1] When the Sixteenth Amendment was before the States for ratification, this Court had held them to be immune from federal taxation except when engaged in "ordinary business activities;" it was doubtless upon their faith in the permanence of the basic immunity that the States elected to ratify the amendment. If this principle of law had existed, the municipalities might not have consented to a reliance on real property taxation as their almost exclusive source of tax revenue. They might not have found it necessary, as a consequence, to place so many of their public projects on a self-supporting basis charging the cost of the facility directly to its users rather than against the general public in the form of general taxes. But the immunity rule was implicit in the Constitution and was never questioned. The fiscal affairs of the States and the municipalities have now been tied indissolubly to that interpretation of the Constitution.

A decision that Congress has the power to tax state and municipal activities, property and income (even apart from tax revenues) would at once impair their credit. Though Congress retained or even expanded all existing statutory exemptions as a matter of federal grace, the mere proclamation of a federal power to tax them would irreparably damage the credit position of the States and municipalities. The revenue laws are revised too often for investors in public securities to place as great a reliance on a statutory exemption as on a fundamental constitutional immunity.

An affirmative answer to the first question asked by the Court on re-argument in this case would at once depress the prices of all outstanding state and municipal obligations and would tremendously increase the interest rates which the

[1] See *Evans* v. *Gore*, 253 U. S. 245, 261 (1920).

States and municipalities would have to pay in all future borrowing. This would not only be because the loss of immunity of the States themselves would inevitably mean the loss of the constitutional immunity of their obligations.[1] Investors would also be faced with the fact that the States and municipalities themselves would be liable to an income tax upon their public works which would greatly reduce the funds available for the repayment of their general obligations as well as their revenue obligations. Thus, a decision upholding the power to tax would impair state and municipal finances even if by congressional forbearance the federal government derived no corresponding revenue benefit.

There are outstanding today about $1,745,000,000 of state and municipal bonds payable principally from the revenues of particular projects and an additional $800,000,000 of special assessment bonds.[2] Furthermore, the entire structure of municipal credit is so interwoven with dependence on charges for municipal services that the whole credit base would be undermined by any proclamation by this Court that the federal government had the power to tax those revenues.

Over the whole country annual non-tax revenues collected by state and local governments amounted to $2,265,645,000 in 1941. This included $1,109,053,000 of non-tax

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[1] The effect of the loss of bond interest immunity is illustrated by the effect of the mere pendency of the question before this Court in *Commissioner* v. *Estate of Shamberg*, 1944 October Term, Docket No. 707. Even though both lower courts had upheld the exemption of the bonds of the agency involved, a recent issue was selling on the morning of January 2, 1945 at 97% of par. Four hours after this Court denied certiorari that same day, the same bonds sold at 100% of par, and within three months the price rose to 103¾% of par. The resulting drop in interest yield attributable to the assurance of exemption was from 2.14% to 1.63%. The reduced rate has resulted in substantial public savings to date in subsequent borrowings of the agencies directly concerned.

[2] U. S. Dept. of Commerce, Bureau of the Census, "State and Local Government Debt: 1941," Table 15.

revenues classed by the Bureau of the Census as "General Government Revenues" including public bridge tolls, and $1,156,592,000 of revenues classed as "Public-Service Enterprise Revenue"[1] including water supply, electric light and power, transit, gas, port facilities and airports.[2] These state and local revenues amounted to fully 20% of all revenues collected by the States and their agencies for their own purposes.[3] In the case of the class of special improvement districts like irrigation and drainage districts, these revenues other than taxes were 47.5% of all the revenues collected by the districts.[4] The five cities in the country with population over a million in 1941 received $381,809,000 of non-tax revenues including $305,990,000, "Public-Service Enterprise Revenue;" New York City's collections in the latter class were $164,198,000 and Los Angeles' were $48,520,000.[5]

Although the revenues from public service enterprises are an important support of the States' economy, their immunity is of no great potential consequence to the federal finances since they constituted only about 1.3% of the $94,500,000,000 total national income in 1941.[6]

If these charges were taxable by the Federal Government, the amount of the tax must be made up, if at all, directly or indirectly from property taxes otherwise available to pay general obligation bonds, with a consequent detrimental effect upon the City's credit. The City of New York has issued about $500,000,000 of general obligation

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[1] U. S. Dept. of Commerce, Bureau of the Census, "Financing Federal, State, and Local governments: 1941" Tables 2, 5.

[2] Bureau of the Census, "City Finances—1942," Table 42.

[3] The total revenues collected by state and local governments apart from fiscal aid from the federal government, amounted in 1941 to $11,370,079,000. See "Financing Federal, State, and Local governments: 1941," cited *supra*, Tables 2, 12.

[4] *Ibid.*

[5] Id. Table 41.

[6] Id. Table 32.

bonds for the construction of its water system. See *Brush v. Commissioner*, 300 U. S. 352 (1937). It has issued $300,000,000 of general obligation bonds for the unification of its transit system in addition to millions of dollars of bonds originally issued for the construction of the system. Although these obligations are technically general obligations, the City looks to water revenues and subway fares for the payment of the interest and amortization upon them. Even the general obligation bonds of the municipalities would be very poor risks indeed if their charges and revenues were to be subject to federal taxation.

It is no answer to say that the States and their municipalities can repair the damage by increasing the charges for their services or their taxes. In most cases that is not at all possible. In the case of municipalities, the only practical possibility for increasing revenues is to increase real property tax rates. The federal government has already pre-empted most of the available forms of new taxation, especially those forms which are progressive in character like the inheritance tax or the income tax.[1] Therefore the property tax has remained the principal source of local tax revenues through the history of local finance in America. At the present time it produces about 80.4% of all local revenues, and about 91.7% of all local tax revenues.[2] Yet it is notorious that the real property tax has practically reached its limit. All recent efforts have been to relieve the burden on real property, particularly in a time when it is so important to encourage a vast increase in new housing. The Court is familiar with the numerous tax strikes throughout the country in the 1930's. Increases in property tax rates in many municipalities have a tendency

[1] 87.4% of all revenues from these taxes in 1941 were collected by the federal government. Local governments, even including the District of Columbia, collected only about 1/10 of one per cent. of the total of such taxes. "Financing Federal, State, and Local Governments: 1941," *supra*, Table 7.

[2] *Ibid.*

to deter the improvement and further development of property, to cause a destruction of older buildings and businesses and a relocation of business and industry.

This Court has itself exploded the myth that there is an inexhaustible reservoir of taxation on which municipalities can draw to meet their obligations. In *Faitoute Iron and Steel Company* v. *Asbury Park*, 316 U. S. 502, 509 (1942), the Court said:

> "The notion that a city has unlimited taxing power is, of course, an illusion."

The law of diminishing returns operates strongly in the field of municipal finance. Increased taxation may mean less rather than more revenues for a city when it has passed the economic ability of many of its taxpayers to meet the tax levy. Delinquency then becomes a more and more serious problem. And with the increase in delinquency, those taxpayers who try to continue to meet their tax obligations must carry the burden of those who have dropped by the wayside. The result is a spiral which leads only to greater delinquency and less revenues and ultimately to bankruptcy.

That process has been demonstrated clearly enough even during a time when municipalities were *not* subject to federal taxation. A Federal Municipal Bankruptcy Act had to be enacted. It requires no imagination to see how infinitely worse would be the following picture if, in addition, the municipalities were saddled with a federal tax on their activities or their property, and particularly on their income:[1]

> "Cameron County Water Improvement District Number One is a public corporation created by the laws of Texas. It has issued bonds for the construc-

[1] Dissenting opinion of Justices CARDOZO, HUGHES, BRANDEIS and STONE in *Ashton v. Cameron County W. I. Dist.*, 298 U. S. 513, 532-4 (1936).

tion of a canal system, which bonds are outstanding in the amount of $802,000. Default has been suffered to the extent of $147,000, either for principal or for interest, upon its obligations now matured. But its own indebtedness is only a part of the financial burden that oppresses it. The bonded debt of other municipalities is a superior lien upon the property in the District for $10,386,000, and accumulated interest. The population is mainly agricultural. The farmers have been unable by reason of the great depression to make a living from their farms, and unable to pay their taxes in appreciable amounts. The District has made diligent effort to enforce collections, but without success. When it has attempted to foreclose its liens, it has been compelled for lack of bidders to buy the lands in and pay the court costs. After buying the lands in, it has been unable to get rid of them, for they have been subject to other tax liens prior to its own. The defaults are steadily mounting. For the year 1932, they were 63%; for the year 1933, 88.9%. The average market value of lands in the District does not exceed $75 per acre; and the total bonded debt per acre, principal and interest, is approximately $100. In these circumstances little good can come of levying more taxes to pyramid the existing structure. The remedies of bondholders are nominal, not real.

"What is true of Cameron County Water Improvement District Number One is true in essentials of thousands of other public corporations in widely scattered areas. The hearings by committees of the Congress before the passage of the statute exhibit in vivid fashion the breadth and depth of the mischief which the statute was designed to remedy. In January, 1934, 2019 municipalities, counties and other governmental units were known to be in default. On the list, which was incomplete, were large cities as well as tiny districts. Many regions were included: 41 out of 48 states. Students of government have estimated that on January 1, 1933, out of securities to the extent of $14,000,000,000 issued by units smaller than the states, a billion were in default. The plight of the debtors was bad enough;

> that of the creditors was even worse. It is possible that in some instances the bonds did not charge the municipalities or other units with personal liability. Even when they did, however, execution could not issue against the property of the debtor held for public uses, and few of the debtors were the owners of anything else. In such circumstances the only remedy was a mandamus whereby the debtor was commanded to tax and tax again. *Rees* v. *Watertown*, 19 Wall. 107, 22 L. ed. 72; *Meriwether* v. *Garrett*, 102 U. S. 472, 501, 26 L. ed. 197, 200. The command was mere futility when tax values were exhausted."

This conclusion was in the minority opinion in the *Ashton* case, but it soon reappeared in the majority opinion in *United States* v. *Bekins*, 304 U. S. 27, 48 (1938). The Court there adopted the language of a California statute, declaring:[1]

> "There exist throughout the State of California economic conditions which make it impossible for property owners to pay their taxes and special assessments levied upon real or taxable property. The burden of such taxes and special assessments is so onerous in amount that great delinquencies have occurred in the collection thereof and seriously affect the ability of taxing districts to obtain the revenue necessary to conduct governmental functions and to pay obligations represented by bonds. It is essential that financial relief, as set forth in this act, be immediately afforded to such taxing districts in order to avoid serious impairment of their taxing systems, with consequent crippling of the local governmental functions of the State."

After quoting this language of the California Legislature, the Court said (304 U. S. 27, 48):

> "While the facts thus stated related to conditions in California, similar conditions existed in other parts of the country and it was this serious situation which led the Congress to enact Chapter IX and later X."

[1] Laws of California, 1934 ex sess., Chap. 4.

Elsewhere in the opinion, the Court said (304 U. S. 27, 53):

> "Improvement districts, such as the petitioner, were in distress. Economic disaster had made it impossible for them to meet their obligations. As the owners of property within the boundaries of the district could not pay adequate assessments, the power of taxation was useless."

The simple fact is that the evolution of state, municipal and federal finance in this country has placed the municipalities in a position where they could not stand the burden of federal taxation. The ability of the States and localities to meet all the needs of their people has been strained to the utmost in recent years. As the record of the depression of the 1930's showed, in many parts of the country, there was a complete breakdown. The shoe, however, was once on the other foot; toward the end of the 19th century it was the federal government which found itself faced with inadequate sources of revenue in order to meet its increasing obligations in the federal sphere. The attempt to meet that situation was made in the Income Tax Act of 1890, which was, however, stricken down by the Supreme Court in *Pollock* v. *Farmers Loan & Trust Co.*, 158 U. S. 601 (1895). When the situation was no longer tolerable, the States were asked to ratify the Sixteenth Amendment to the Constitution permitting the federal government to enact effective income tax laws. The needs of the federal government were recognized by the States at that time, and the federal government has never again been lacking in the means to meet its every financial need. The States submit that now, when local government is so close to the limit of its ability to raise revenues to provide for the public welfare, the federal government should not be permitted to increase the burdens of the States.

The effects of impairing municipal credit do not stop with the municipalities themselves. If this case or any other case even suggested that the federal government has

power to tax state and municipal incomes, the values of their outstanding securities would be sharply depressed. Yet these securities are largely held in public sinking funds, by banks and insurance companies and by federal agencies like the Reconstruction Finance Corporation.[1] These are institutions in which the public has a great stake.

In considering the social aspects of a reversal of precedent in this field, it should not be forgotten that of the tax monies paid by persons in the lower income levels, by far the greater part is paid to local government, particularly to municipal government. Under 1946 income tax rates the normal family of four with an income of about $2200 will pay no income tax whatever. The federal government collects very little in taxes from this family: merely taxes on admissions to moving pictures, on cigarettes, and on an occasional purchase of small luxuries. Even the Social Security Tax, although only one per cent, is considered a form of insurance. But this same family, if it owns its own home with a value of about $5000, will pay local real estate taxes of about $150 to $200 a year (plus charges for water and perhaps gas or electricity furnished by the city). The fact is that progressive income and inheritance taxes have been largely pre-empted by the federal government. This leaves municipal government supported more than any other by low incomes and it leaves the low income earner supporting municipal government more than any other government. A change in constitutional law which transfers millions of dollars annually from municipal treasuries to the federal treasury must be regressive in its result, bearing down most heavily on those least able to afford it.

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[1] In 1942 at least 60% of all state and local obligations were held by owners other than private individuals and commercial corporations. Government funds owned 25.1% of all outstanding; banks owned 20.3%; insurance companies 10.8%; and tax-exempt institutions other than mutual savings banks held 3.1%. Annual Report of the Secretary of the Treasury, for fiscal year ending June 30, 1942, Table 100.

The economic inability of municipalities to finance much needed regional improvements out of tax revenues was an important element in the development of revenue financing of public works. Another reason was the conviction that many public improvements do not benefit all taxpayers equally, some receiving benefits from a public project and some none at all. It was only equitable to accommodate the charge for the service to the benefit derived. The result was to pay for the cost of the improvement out of charges against the actual users of the facility instead of against taxpayers generally. This form of government financing has done much to relieve the hardships caused by the inelasticity of the local fiscal systems; it has produced vast public improvements which could not have been provided on any other basis. Annual revenues from projects of this sort increased 122.5% from $519,807,000 in 1932 to $1,156,592,000 in 1941.[1]

Federal taxation of the income of such facilities would not only be interference; it would be complete destruction. They are financed out of the proceeds of bonds payable primarily from the revenues of the project yet to be built. The investor, and not the public provides the initial capital. He will not do so unless he is convinced that the revenues of the project are likely to cover all operating costs, all interest costs, the cost of amortizing the debt over a reasonable period of time, and a margin of coverage to allow for possible errors in calculation and for periods of economic depression.

All state and municipal revenue bonds are issued on the basis of immunity of the public income from federal income taxes. They make no provision for the payment of such taxes. Their debt service requirements are calculated carefully at the time of inception of the project to absorb practically all their surplus revenues over operating costs with

[1] "Financing Federal, State, and Local Governments: 1941," *supra*, Table 12.

only sufficient margin to meet the requirements of investors. Since their purpose is to pay off the debt as soon as possible to provide free or low cost public service, the schedule of debt retirement is naturally accelerated as far as possible commensurate with the anticipated income over operating expenses only. If they must pay federal income taxes on their surplus revenues before deduction of debt retirement expenditures, they could not possibly meet their debt service requirements.

Not only would this mean the bankruptcy of such projects as have already been built on a self-supporting basis, but it would put an end to this method of state financing. Investors are not likely to advance their money to such undertakings if the margin of safety is drastically reduced by the annual payment of federal income taxes out of revenues which otherwise would be available for debt retirement. They will require, instead, general obligations supported by a pledge of the state or municipal taxing power. This is particularly so because the financing of these public improvements is so often of a marginal nature.

7. Effect of Reversal of Precedent on the Federal Government.

Indeed, the rule which would permit "non-discriminatory" taxation of government agencies would have violent repercussions on the federal government. The doctrine that all constitutional federal activities are governmental and therefore immune, has protected the federal government from taxation by the States. *Pittman* v. *Home Owners' Loan Corporation*, 308 U. S. 21 (1939); *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95 (1941). But if even governmental functions are to be subject to non-discriminatory taxes, the federal government must prepare to pay real estate taxes at regular non-discriminatory rates on every federal post office, arsenal, court house, or office building; to pay regular non-discriminatory record-

ing taxes on every federal deed or mortgage, issuance taxes on federal bonds, sales taxes on federal purchases and income taxes on the surpluses produced by government agencies. (*Cf.* dissenting opinion in *James* v. *Dravo Contracting Co.*, 302 U. S. 134, 178-180.)

The total annual federal revenue from such federal credit corporation and public service enterprises in 1941 according to the Bureau of the Census was $1,491,346,000, derived from the following federal agencies or projects:[1] "Alaska Railroad, Alley Dwelling Authority, Banks for Cooperatives, Boulder Dam (power and water), Commodity Credit Corporation, Defense Housing, Disaster Loan Corporation, Electric Home and Farm Authority, Export-Import Banks, Federal Crop Insurance Corporation, Federal Farm Mortgage Corporation, Federal Housing Administration, Federal Intermediate Credit Banks, Federal National Mortgage Association, Home Owners' Loan Corporation, Panama Canal, Post Office Department, Production Credit Corporation, Public Works Administration (in respect to power and other utilities), Reclamation Bureau (in respect to power aspects), Reconstruction Finance Corporation, R. F. C. Mortgage Company, Regional Agricultural Credit Corporation, Rural Electrification Administration, U. S. Housing Authority, Tennessee Valley Authority (in respect to current power operations)." In addition the Bureau of the Census reports $463,697,000 of other federal non-tax revenues in 1941.[2]

We have submitted in this Point that the federal system is worth preserving and that the destruction of the States would be a calamity.

We have shown, even considering the question *de novo* without reliance on precedent at all, that the detructive

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[1] "Financing Federal, State, and Local Governments," *supra*, Table 11.

[2] Id., Table 2.

impact of federal taxation of the States would be real and actual. It would operate through the power of selective and conditioned exemption to substitute federal policy for local policy in matters of purely local concern.

It would operate to destroy local government by curtailing its ability to afford essential services and at the same time compelling it to shoulder a great federal tax burden. These are arguments which lead to the conclusion that the federal government does not have and should not have constitutional power to tax the States whenever they are engaged in the performance of public activities essential for the best interests of their people.

Certainly the disastrous consequences of taxing the activities which the States and Cities have been carrying on up to the present time are such as to place that proposal in the category of constitutional revision rather than constitutional interpretation. The fact is that the States and municipalities could not accommodate their finances to federal taxation of their income from their water supply, highways, bridges, hospitals, piers, municipal power plants, terminals, irrigation systems, traction systems, drainage developments, sewers, and all the other activities they have already undertaken on a revenue basis in answer to public need. Certainly these activities must continue immune from federal taxation even though non-discriminatory.

POINT II

An examination of the rule which permits federal taxation of the States only when actually necessary to preserve the existence of the Union.

The problem of intergovernmental taxation arises from the dual nature of our government and from the premise implicit in the Constitution that both the state governments and the national government are vital to the public welfare.

In passing it may be stated that the validity of this premise is not open to debate.[1] Local self-government—the right of the people of a State to decide all matters of state concern and the right of the people of a city or other locality to decide all questions of local concern—is obviously of the essence of any liberal and democratic system of government. If this premise is invalid then the time has come to call a general constitutional convention to recast the entire system of government.

The premise from which to start is therefore that both the States and the Union must be preserved. As applied to intergovernmental taxation this raises two questions:

(a) How far *must* the federal government actually go in taxing the state governments in order to preserve its own existence.

(b) Similarly, how far *must* the state governments actually go in taxing the federal government in order to preserve their own existence.

It will be noted that the first of these two questions differs fundamentally from the question which is sometimes raised as to how far the federal government could go in taxing the States without destroying them. Apparently this last question springs from Judge MARSHALL's dictum that the power to tax involves the power to destroy, and through some mistaken chain of reasoning, from the conclusion that anything short of total destruction is constitutional.

The two questions posed above are, however, more in accord with public policy as well as with constitutional principles. They recognize, as does the Constitution itself, that local self-government is of the essence in any liberal and democratic system, and they also recognize the fact

[1] See *supra*, pp. 14-19.

that it is equally essential to have a strong and vigorous national government to cope with foreign affairs and with those internal affairs where uniformity throughout the nation is necessary.

The mere statement of these questions is sufficient to provide their answer. Bearing in mind that vast reservoir of private property,[1] activities and income[2] which is subject to the taxing power of both the States and the Nation, no argument is necessary to demonstrate that there is no actual necessity for either to tax the other in order to raise sufficient revenue to carry on its affairs, nor, as a practical matter, is there any real likelihood that such a situation will ever materialize. As pointed out elsewhere in this brief, the federal government has raised enormous revenues during the war years—many times the amount that some fiscal experts thought possible—without collecting any material amounts from the States. From the standpoint of the necessity of preserving the federal government, no taxation of any state activity, property or income is now justified or is ever likely to be justified.

1. Advantages of the Rule: Expediency, Soundness and Reciprocity.

The rule above derived from the Constitution is that federal power to tax the states (and state power to tax the federal government) exists only if and when all private sources of tax revenue are exhausted and definite proof is made that intergovernmental taxation is actually necessary to provide sufficient revenues to carry on the affairs of the taxing government,—a situation which as a practical matter we believe will never arise. This rule has the additional

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[1] The assessed valuation of property subject to taxation for State or local purposes in 1940 was $144,636,317,000. "Property Taxation: 1941," *supra*, Table 11.

[2] The national income in 1941 was $94,500,000,000. "Financing Federal, State, and Local Governments: 1941," *supra*, Table 37.

virtues of practicability and expediency. It avoids all those distressing and unsatisfactory attempts to classify state activities between the immune and the taxable; it is a rule which will forever rid this Court of the plague of immunity cases like the instant case. It has the great advantage of freeing this Court from any duty to inquire into the motives of the State Legislatures. It meets the objections raised in Point I. It avoids the repugnance between taxation and the sovereignty of the government taxed. It eliminates the possibility of taxation as an instrumentality of destruction through control, and taxation to prevent the States from exercising the full measure of their sovereign powers. And it satisfies the fundamental point that special privilege for the federal government as against the States is inconsistent with a truly federal system.

Reciprocity and equality were the uniform policy of this Court from the beginning. If the dictum in *Helvering* v. *Gerhardt*, 304 U. S. 405, 412 (1938), implies abandonment of that constitutional rule, it is not justified by the paragraph from *M'Culloch* v. *Maryland*, 4 Wheat. 316, 435, 436 (1819), cited in the *Gerhardt* opinion. The next paragraph in Chief Justice MARSHALL's opinion, which was not quoted in the *Gerhardt* case, supplies the answer.

On the argument the State of Maryland had assumed that state banks might be taxed by the federal government. Since the taxing powers of both the States and the Nation are concurrent, the State therefore contended that it might likewise tax the bank of the United States.

Pinckney, arguing for the bank's immunity, gave two alternative answers:[1] first he argued that the federal and state governments were essentially different, implying that the federal government might well be immune from state taxation, even should state instrumentalities be taxable by

[1] 4 Wheat. 316 (1819).

the federal government. But then he argued alternatively that the State of Maryland was wrong in assuming that the federal government had the power to tax the state banks. True, the state and national taxing powers were concurrent, he said. But that did not mean that the bank of the United States was taxable, he concluded. *It might prove rather that the state banks were immune.*

Chief Justice MARSHALL *accepted his reasoning in toto* and, at the close of his opinion, he rejected the State's argument on this point. Its assumption was wrong: the concurrence of the taxing power did not prove reciprocal taxation, he explained; *but it might prove reciprocal immunity.*

His language is:[1]

> "But if the full application of this argument could be admitted, *it might bring to question the right of Congress to tax the state banks,* and could not prove the right of the states to tax the Bank of the United States."

Chief Justice MARSHALL's alternative suggestion of reciprocal state immunity could not be tested until the federal government adopted the internal revenue act of 1864. From that time on reciprocity and equality were always supported by this Court. The rule has always been: "That immunity is implied from the nature of our federal system and the relationship within it of State and national governments, and is equally a restriction on taxation by either of the instrumentalities on the other." *United States* v. *California*, 297 U. S. 175, 184 (1936). A few of the other many expressions of the reciprocity and equality of the immunity are found in *Ambrosini* v. *United States*, 187 U. S. 1, 7 (1902); *Metcalf* v. *Mitchell*, 269 U. S. 514, 522 (1926); *Indian Motocycle Co.* v. *United States*, 283 U. S. 570, 575 (1931).

[1] 4 Wheat. 316, 436; Italics supplied.

It is difficult to see any sound reason to depart from this rule at this time when the necessity of the change is not pressing and the result is merely to subordinate the state government to the federal government.

2. The Fallacy of Curtailing State Immunity to Enhance Federal Revenues.

We have searched the cases to find what the practical objection is to complete immunity of state activities. We have found only one practical objection stated: that the complete immunity of all activities within the power of the States might jeopardize the existence of the federal government by eliminating revenues which might otherwise be collected. The rule suggested above fully meets this objection.

Furthermore, the almost limitless ability and resources of the federal government in raising revenues, as those abilities and resources have been demonstrated through the past ten years, effectively dissipates the notion that any forseeable activities of the States can seriously impair the ability of Congress to raise adequate revenues.

a. Incidental Deprivation of Revenue Is Not Decisive.

The argument for the limitation of state immunity to keep federal revenues intact is nothing but the old argument against an economic burden. It has been discarded in the field of derivative immunity. The case of *Graves* v. *Texas Co.*, 298 U. S. 393 (1936) decided an immunity question on the basis of cost burdens. *Alabama* v. *King & Boozer*, 314 U. S. 1 (1941) rejected that doctrine. If neither the States nor the federal government can any longer claim immunity merely because the tax costs them money, it is difficult to see why the federal government should still be permitted to tax the sovereign States merely because not to do so would cost the federal government money.

The latest cases involving intergovernmental immunity reject any qualification of federal immunity.[1] The result in those cases was foreshadowed by *James* v. *Dravo Contracting Co.*, 302 U. S. 134 (1937). And those latest federal immunity cases, in turn, foreshadow the abandonment of the classifications stemming from *South Carolina* v. *United States*, 199 U. S. 437 (1905), which have no better basis than the same "cost" argument.

b. *The Offset Against Federal Revenue "Losses."*

Even if this Court had never wavered from the economic cost test of immunity, the objection to state immunity which talks about the necessity of preserving federal revenue sources would still be completely untenable. Its most glaring fault is that it looks at only one side of the balance sheet. No effort has ever been made, in discussing federal revenue losses through state immunity, to consider how much the States' activities have increased federal revenues by improving the prosperity and income of the people of the States from whom the federal government derives its revenue.

Certainly the tax potential of the federal government is a mathematical function of the welfare and prosperity of the people of the Cities and States of America. The sole purpose of the functions and activities of the States is to promote that welfare, health and prosperity. American prosperity and the national credit of the federal government is testimony to the fact that the States and Cities have played their full contributing part to the national economy. The people of a municipality elect to distribute their own water, to operate their local transit facilities, or to take over their local gas plant because of the people's conviction that in public hands service can be improved,

[1] *Pittman* v. *Home Owners' Loan Corp.*, 308 U. S. 21 (1939); *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95 (1941); *City of Cleveland* v. *United States*, 323 U. S. 329 (1945).

rates can be reduced and the facilities can make a greater contribution to the welfare and prosperity of the people of the locality. When those public objectives are attained, the federal government gains much more, tax-wise, than it may theoretically lose through the loss of taxation of the private company which may formerly have operated the water works, the transit system, or the gas plant.

Chairman Lilienthal of the Tennessee Valley Authority recently reported that the activities of that agency have increased the per capita income payments in Tennessee from $190 a year in 1933 to $317 a year in 1940 and finally to $764 in 1944. The increase was 67% to 1940 and 302% to 1944. That this was attributable to the federal determination to enter the utility field in the Tennessee Valley appears from comparison with equivalent figures for the United States as a whole. The country-wide per capita income payments increased only 204% from 1933 to 1944, as compared with 302% for Tennessee alone. This great gain in the local tax base must be offset against the loss of taxes by the federal government's acquisition of the Tennessee Electric Power Company in 1939.

Obvious benefits have accrued to the federal income tax revenues as a result of the increase in business and the prosperity of the New York metropolitan region brought about through the construction by New Jersey and New York of the great bridges and tunnels crossing the Hudson River and linking New York with the great industrial region of Northern New Jersey.[1]

In 1927, before New York and New Jersey completed the Holland Tunnel under the Hudson River, trans-Hudson traffic amounted only to 2,500,000 vehicles a year. Today, trans-Hudson traffic through the Holland Tunnel, Lincoln Tunnel and across the George Washington Bridge has risen to approximately 30,000,000 vehicles per year.

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[1] See *Commissioner v. Estate of Shamberg*, 144 F. (2d) 998 (1944), cert. den. 89 L. ed. Adv. Ops. 282 (1945).

In other words, the new inter-state highways under and over the river largely created their own traffic and provided a great stimulus to the commerce of the Port of New York District. Many additional millions of dollars of federal gasoline tax were collected by the federal government because of these new state facilities. Millions of dollars of additional income tax were collected by the federal government because of the tremendous savings effected by businesses using these highways; they have lowered the average toll paid by businesses crossing the Hudson, they have eliminated wasteful congestion which made many man-hours of work completely unproductive, they have effected a great saving in the time and costs necessary to cross the river; they have created a great new suburban bus industry; they have been directly responsible for much new suburban home building; they have, in short, greatly increased the prosperity and income level of business and persons in the New York and New Jersey and increased the wealth of a great number of federal taxpayers.

Most new state services produce the same result. A better regulated liquor dispensing system in Ohio may have well produced a healthier and more prosperous community which paid more federal income taxes because of the State's activity. This may well have increased federal revenues more than state immunity would have decreased them. The Bank of North Dakcta, established by constitutional amendment, has done much which could not have been done by private institutions, to promote the general prosperity of the people of that State.

The wealth of the largest city in the country, from which the federal government draws a large share of its tax revenues, would not be possible if it were not for the municipal transit system upon which the City has spent over $1,300,000,000. The City could not have grown in size and in wealth if rapid transit had not been provided to

connect its business heart with its far-flung residential areas. The City built the entire system itself. For years portions of it were operated under leases with private operators, but the people ultimately felt that the service thus provided was inadequate. Pursuant to a popular referendum, the City ultimately took over the entire operation itself.

As examples multiply, it becomes absurd to talk of the losses of federal revenue from state activities. The loss is certainly not a net loss. The Erie Canal created wealth in the middle-west and in New York, which has never ceased to profit the federal government in tax sources. The Department of Water and Power of Los Angeles has provided the water and power which made possible a great new metropolis, whose wealth has never been a source of regret to the federal tax collector.

The construction of public projects by the States has also provided employment on a large scale and thus, in times of economic stress has helped to relieve the burden of the federal government in caring for the unemployed. Taxation of the States which would limit their ability to continue construction of such projects would cast a far heavier burden on the federal government in the necessity of caring for the unemployed than the federal government would lose because of the immunity of the States in undertaking their activities.

c. *The Groundless Fear of State Expansion and Socialism.*

Possible loss of federal tax revenue as an objection to state immunity was first voiced in *South Carolina* v. *United States*, 199 U. S. 437 (1905). It ignored the broader considerations of public policy, public welfare and public prosperity pointed out above. But what is more, it was based upon three fears which the passage of forty years have absolutely dissipated.

These were fear of an enormous expansion in state activities which had previously yielded federal revenue, fear of socialism and fear that the federal government would not be able to survive the anticipated expansion by the States.

The expansion of state activities into new fields has not been great. The States have provided public services in cases which were financially marginal but where the public need existed and private capital was not capable of filling it. Of course, in these cases, if the State did not act, the services would not exist at all so that there is no real loss of federal revenue because of the State's immunity. Another class of case involves certain natural monopolies like water, power and traction. The States and municipalities generally come into these fields when the service provided by private persons prove inadequate. See *Brush v. Commissioner*, 300 U. S. 352, 360 (1937). In other words, it is rarely a choice between State operation and private operation. In most cases it is rather a choice between State services and no service. The liquor business in South Carolina in 1905 may itself be an example. Apparently the private liquor traffic had resulted in so many evils that the people would no longer tolerate it. Had not the State substituted the dispensary system, the people might well have considered complete prohibition the only alternative. In that case the federal government would have lost no more revenues than if the State's immunity had not been restricted.

The results of the Public Utility Holding Company Act of 1935 gave an excellent example of the baselessness of the fear that there was a movement toward public ownership of utilities to an extent that could in any real degree jeopardize federal revenue bases. (See *South Carolina v. United States*, 199 U. S. 437, 454 (1905).)

The "death sentence" provision of the Act has compelled many public utility holding companies in the past few

years to dispose of their local operating properties. Some persons, perhaps because they disagree with the purpose of the Act, or perhaps out of dislike of public ownership, have complained that the federal legislation combined with the States' tax immunity was resulting in a widespread movement toward public acquisition of private power plants. Yet, as this brief is written, Chairman Ganson Purcell of the Securities and Exchange Commission, has testified before the Subcommittee of the Committee on Interstate and Foreign Commerce of the House of Representatives that this is absolutely not so. He testified that of all the local public utility operating properties that have been sold as a result of the Federal Act, about $4,053,719,000 worth were sold to private interests and only about $293,500,274 worth was purchased by government agencies; and of that latter figure the federal government itself acquired almost half represented by sales to the federal Tennessee Valley Authority.

The fact of the matter is that the movement toward state and municipal ownership has never reached the alarming proportion and the variety of fields which was feared in 1905. It has never extended to "tobacco, oleomargarine and all other objects of internal revenue tax." *South Carolina* v. *United States*, 199 U. S. 437, 451 (1905). As a matter of fact, the extension of activities by the federal government has far outstripped any corresponding extension by the States. And yet the incidental loss of local tax sources was not considered an objection to complete federal immunity in *Pittman* v. *Home Owners' Loan Corporation*, 308 U. S. 21 (1939) or in *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95 (1941).

Fear of socialism was obviously another great reason for the limitation of state immunity in 1905. The Court in the *South Carolina* case expressly stated that that was one of the impelling reasons for the decision (199 U. S. 437, 454, 455). It would seem utterly unnecessary for us to

enter here into a discussion of how unfounded was that fear in the light of the history and development of our States over the past forty years. We should observe, however, that the confusion in this constitutional field over the past forty years might very well be traced to this introduction of these considerations of political philosophy into the field of intergovernmental taxation. The perversion of the federal taxing power to an instrument for curbing the political tendencies of the States could only have resulted in judicial confusion.

d. The Impregnable Position of Federal Finances.

If in 1905 there was any justification for a fear that state immunity might impair federal revenues to any substantial degree, it was certainly ended by the 16th Amendment which permitted effective federal income taxation beginning in 1913. The history of federal finances in the past four years contains the decisive answer. The colossal increase in federal revenues to meet the greatest fiscal emergency of all times hardly squares with the picture of a weak and decrepit federal government being starved to death by a crippling loss of revenues because of state immunity. Any government with the demonstrated capacity of our federal government to multiply its revenue over and over again, hardly fits the picture painted by the fears of 1905. Federal tax revenues jumped from $1,891,290,000 in 1932 to $7,818,365,000 in 1941.[1] By 1945 it had reached the staggering total of $46,456,554,000.[2]

The fact of the matter is that the federal government has never collected an income tax on state revenues. It has never collected a property tax on state property. It has never relied upon the States as a substantial source of

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[1] "Financing Federal, State, and Local Governments; 1941," *supra*, Table 9.

[2] Fiscal year ending June 30, 1945. See Daily Statement of the Treasury Department, June 30, 1945.

tax revenue. The activities of the States have not imperiled the ability of the federal government to raise adequate revenue. Whatever activities the States are actually likely to go into in the future will do as little harm to the stability of the federal government as have their activities in the past.

There was much more substance to the fear of loss of federal revenues when derivative immunity was more freely allowed. Now that the claims for immunity by state and municipal employees, contractors and lessees have been finally rejected (see *Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466 (1939)) the loss to the federal government from state immunity is only a fraction of what it would have been in previous years.

There is no inherent vice in the fact that state or federal activities may cut down the corresponding federal and state tax sources. That happens every time the federal government buys real estate to erect a postoffice or a federal power development, or river front property for the operation of federal barges in commercial service on the Ohio or Mississippi. Here the loss of real estate taxes to the locality is immediate and measurable. Presumably, however, the community or the region derives more public benefit and the enhancement to the public welfare and prosperity far out-weighs the measurable real estate tax losses. The same principle operates where in order to construct a reservoir or a dam or a toll highway, the state government buys property theretofore devoted to income producing uses in private hands. It is difficult to conceive that a different principle applies where the people of a State or locality, in the interest of the local welfare and prosperity, take over a privately owned water system or toll bridge or gas plant. For reasons which we have hereinbefore stated, we believe that by the enhancement of the general health, welfare and prosperity of the locality, the strength and resources of the federal government are immeasurably increased.

The States can, by the exercise of their regulatory power, substantially reduce federal tax revenues in many ways. Prohibition of intoxicating liquor would as effectively have eliminated federal revenues from the liquor traffic in South Carolina as state immunity would have done. A State may regulate rates charged by public utilities and thus lessen their income and the income tax they will pay the federal government. A State may fix the hours of closing places of amusement and thus curtail the federal receipts from its cabaret tax. A State may prohibit moving pictures on Sunday and thus curtail receipts from the federal admissions tax. The loss of federal revenue has never been urged as a reason for curtailing the state power to regulate. It is no better reason for curtailing state immunity.

Any actual danger that state immunity will seriously injure the federal government by withdrawing federal revenue sources is non-existent. Such an incidental loss of money has ceased to be an objection to immunity, and is more than offset in dollars and cents by the federal tax gain from the prosperity created by state activities. Above all, the real danger to the balance of the federal system and the survival of the States which would arise from taxation of the States is too serious to be outweighed by the flimsy argument against "withdrawal."

The only constitutional interpretation consistent with our federal system is one which would permit federal taxation of the States only if and to the extent such taxation is actually (and not hypothetically) necessary to preserve the federal government from destruction due to proven inability to raise necessary revenues because of the immunity of state activities. The axiom of constitutional law that both the States and the Union must be preserved intends the preservation of the States as fully effective entities for the promotion of the public welfare. It is wholly inconsistent with a conclusion that the federal government may tax the

States so long as some undefined remnant of state government is not destroyed. Upon this basis there is no scope for limitation of state immunity at the present time or under any future conditions which can possibly be expected to materialize. The States are not taking over all private business, and the federal government without the necessity of taxing the States, will still remain financially the strongest government in the world. We need not speculate on the fantasy of a decrepit federal government and overreaching States. Yet only such fantasy justifies a limitation on state immunity.

POINT III

An examination of the rule holding that "governmental" activities undertaken by the States are immune from federal taxation.

It has already been demonstrated that to subject the States generally to federal taxation even though technically "non-discriminatory," would be incompatible with constitutional principles and sound public policy. We have also discussed the extent of the limitation upon state immunity which is required by the necessity of protecting the continued effectiveness of the federal government. There remains for discussion, however, the distinction sought to be made in many opinions between "governmental" and "non-governmental" activities. An analysis and careful consideration of this attempted distinction makes three points clear:

First, that any rule which seeks to limit state immunity to the specific methods used by the States in meeting public needs, in 1789 ignores the fundamental necessity of adapting governmental procedures, practices and activities to changing circumstances and would reduce the States to primitive

colonial governments incapable of meeting modern social and economic conditions.

Second, that any rule which seeks to restrict state immunity to "normal," "customary" or "usual" activities, meets with the insuperable difficulty which this Court has already encountered, that if the terms are taken overliterally it is impossible as a practical matter to determine what they mean.

Third, that any rule which would seek to confine the States' immunity to "essential" governmental activities, if the phrase is taken over-literally, involves the fallacy that there is some irreducible minimum of state activities, which constitute the soul or essence of state government and that all else is surplusage.

In truth, the real difficulty seems to be with the word "activity." If the word means a specific operation—driving a horse as contrasted with driving an automobile—then the difficulties indicated above exist. In 1789 the States engaged in the promotion of public welfare, but the particular methods and procedures by which they did so were those of a century and a half ago. If, however, the word "activity" refers to the end rather than the means—if it is the promotion of the public health and all steps taken to that end which constitute an "activity,"—if the operation of an X-ray machine and of a fluoroscope are not deemed separate activities—then no difficulty is encountered.

If state immunity is to be tested by the nature of the state activity, then as will appear, the only practical and workable rule is that those activities undertaken by the State for the purpose of promoting the public welfare, health and safety are *per se* "essentially governmental" in the true sense of the term and immune from taxation, together with the property used in such activities and any income incidentally derived therefrom.

1. The True Nature of the Various "Governmental" Function Tests.

Some of the cases suggest that there may be a difference between a "governmental" activity and a "business," "commercial" or "non-governmental" activity. *South Carolina* v. *United States*, 199 U. S. 437, 461 (1905); *Flint* v. *Stone Tracy*, 220 U. S. 107, 157 (1911); *Ohio* v. *Helvering*, 292 U. S. 360 (1934); *Helvering* v. *Powers*, 293 U. S. 214 (1934); *Allen* v. *Regents*, 304 U. S. 439 (1938). Here the idea seems to be that some things which a government does are "governmental" and other things are not.

Elsewhere in the opinions the approach is in terms of what we may call "grades of governmentality." Here we have the many adjectival tests which seek to determine whether an activity is a "strictly governmental function,"[1] an "ordinary governmental function,"[2] an "essential governmental function,"[3] a "necessary governmental function,"[4] a "usual governmental function"[5] and a "traditional governmental function."[6]

Each of the two possible approaches will color the answer. Thus, the group of tests which talk of "ordinary," "traditional" and "usual" governmental functions, have been discussed from two points of view. *United States* v. *California*, 297 U. S. 171 (1936), concedes immunity "to the activities in which the states have traditionally en-

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[1] *United States* v. *Baltimore & Ohio R. R. Co.*, 17 Wall. 322, 329 (1873); *South Carolina* v. *United States*, 199 U. S. 437, 461 (1905); *Ambrosini* v. *United States*, 187 U. S. 17 (1902); *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 157 (1911).

[2] *United States* v. *Baltimore & Ohio R. R. Co.*, 17 Wall. 322, 329 (1873); *South Carolina* v. *United States*, 199 U. S. 437, 451, 459 (1905).

[3] *Flint* v. *Stone-Tracy Co.*, 220 U. S. 107, 157 (1911).

[4] *Metcalf* v. *Mitchell*, 269 U. S. 514, 522 (1926).

[5] *Helvering* v. *Powers*, 293 U. S. 214 (1934).

[6] *United States* v. *California*, 297 U. S. 175, 184 (1936).

gaged." But *South Carolina* v. *United States*, 199 U. S. 437, 458 (1905), would withhold immunity from an activity "which ordinarily is carried on by individuals." Yet there are dozens of activities which in one sense are both "traditionally governmental" and also "ordinarily carried on by individuals." The parallel is clear between the Federal Land Banks or The Bank of North Dakota and private banks, the United States Employment Service and private employment agencies, the Nevada Industrial Commission administering workmen's compensation insurance and the Aetna Casualty Insurance Company, the Los Angeles Department of Water and the Hackensack, New Jersey, Water Company, the United States Post Office and the Railway Express Agency, the Detroit Street Railway System and the Philadelphia Rapid Transit Co., The Golden Gate Bridge and a private toll bridge, the Springfield Arsenal and the United States Steel Company.

Here again we are driven to the only possible distinction:—the objective of the government on the one hand and the private company on the other. Thus it is fair to say that it is a "traditional," "usual," and "normal" function of government to provide whatever services are necessary to promote the public welfare, health and safety, but that it is *not* a traditional objective of private business.

In this way we are spared in the case of the States, as we are in the case of the federal government, the necessity of trying to work out a logical system of categories. We are spared the necessity of trying to decide whether the construction of a state capitol is a "usual governmental function" or is simply the "ordinary business" of building construction. We are spared the necessity of trying to decide whether vehicular tunnels are "ordinary governmental activities," because governments have traditionally built bridges, although tunnels are a relatively new engineering technique. We are spared the necessity of making a host of aggravating distinctions, which, we have shown, have

no relation to the preservation of the federal and the state governments.

We are particularly spared the problem of deciding how many years it takes to make a tradition, what percentage of government participation in a field makes it a "usual governmental function," and whether a function becomes "usual" as time goes by and the percentage increases. We are not troubled with the question whether some earlier time in history should be chosen rather than our own as a vantage point from which to decide what are "traditional" and "usual" governmental activities. And we are spared the problem of "individual philosophies" in deciding, apart from the decision of the people of the States, just which activities are "essential" and which may be dispensed with.

We are forced to conclude, like the Court before us in *Brush* v. *Commissioner*, 300 U. S. 352, 361 (1937), that these adjectives do not constitute a rule because they are not "used as an exclusive or rigid delimitation." Each of them is capable of a wide range of interpretations from the narrow to the broad. After studying all of them, we are drawn to the conclusion that none of them is inconsistent with the rule which we have advocated; in their true sense each leads to the same conclusion, that immunity is at least co-extensive with activities undertaken by the State with the primary motive of improving the public health, safety and welfare.

The judicial attempts to distinguish between "governmental" activities on the one hand and "business" or "commercial" or "non-governmental" activities on the other, have not been successful. To the Court of the *South Carolina* case, supplying potable water was an ordinary business operation;[1] to the Court of the *Brush* case, it was an "essential governmental function."[2] We know no

[1] 199 U. S. 437, 451 (1905).
[2] 300 U. S. 352 (1937).

touchstone which distinguishes the sheep from the goats in this field. One dictionary definition of a "business" is "any particular occupation or employment habitually engaged in especially for livelihood or gain." "Commercial" is defined as "having financial profit as a primary aim."

These dictionary definitions loosely fit the popular use of the words; they seem to fit the thinking underlying the Court's decision in the *South Carolina* case. In a democracy people do not think of the activities undertaken by their governments for the primary purpose of promoting their welfare, as "business" or "commercial." They do not think of the postoffice as a "business," but they do think of the American Railway Express in those terms. They don't think of the Bronx Zoological Park as "commercial," but they do class the Barnum and Bailey Circus in that category. The Home Owners Loan Corporation or The Bank of North Dakota is not popularly considered a business activity, but the corner bank is. We do not consider the Nevada Industrial Commission which furnishes workmen's compensation insurance as a business operation, but even a mutual life insurance company is considered just that. The United States Employment Service and the corresponding state services are not "businesses" in popular thinking, but a private employment agency is considered "commercial."

The only possible reconciliation of these attitudes has already been pointed out:—it is the difference in objective between the public and the private operation. If the public operation is undertaken to provide a service which the State or the federal government considers necessary, it cannot be considered a "business" in the popular sense of that term. Government is the antithesis of business in the sense that government seeks to provide services and it makes charges only as an incident thereto, while business provides services only as an incident to making profits.

It seems as fruitless to attempt to classify various degrees of "governmental function" as to distinguish between "governmental functions" and "business" or "commercial" activities, except in terms of the objective of the government providing the service. The various adjectival tests seem to form into groups. One group talks in terms of "ordinary," "customary," "traditional," "usual" "governmental functions." The aim here apparently is to protect the federal government from what was once feared would be a loss of revenue sources. The other group talks in terms of "strictly," "essential," "indispensable" "governmental functions" and apparently conceives that there is some irreducible minimum which constitutes the essence of state government and that all else is surplusage.

This is the choice of attitudes: either to protect the maximum value of the States or to protect an irreducible minimum of states activities. The first attitude accepts forebearance and immunity as a normal concept and countenances exceptions in the rule only where the States go beyond those activities undertaken to promote the public welfare. The second attitude assumes taxation of the States to be a desirable federal power and grudgingly concedes only sufficient immunity to permit States activities within some irreducible minimum essential to survival. Perhaps these differences in approach explain some of the conflicting writings on the questions.

Our interpretation of the "traditional-usual" "governmental function" tests meets the paramount need of the people of the States that state government shall not be stagnated. Any other interpretation would place the States in a straitjacket and freeze their activities as of some point of time. Yet, as Mr. Justice BLACK said in his concurrence in the *Gerhardt* case:[1] "The genius of our government provides that within the sphere of constitu-

[1] 304 U. S. 405, 427 (1938).

tional action, the people—acting not through the courts but through their elected legislative representatives, have the power to determine as conditions demand, what services and functions the public welfare requires."

Some of the cases have suggested that we may have no more modern viewpoint than that of 1776 or 1789 in appraising the traditional or usual character of "governmental functions."[1] It cannot be that in this single field the clock is not only to be stopped but is to be turned back a century and a half. The question cannot be answered by saying that port and harbor development is a governmental activity[2] but that airport development is not. In other words, the answer is not in terms of the specific machinery, or even, if you will, in terms of the specific activity by which the State or the federal government seeks to achieve its governmental purposes. The founding fathers were men of broader vision. They intended that State governments would continue to exercise "traditional" and "usual" and "essential" governmental functions by continuing to serve the welfare of their people in any way within their constitutional power.

It was for this reason that the Court had no difficulty in the *Brush* case in classing as "governmental" an activity which the City of New York did not begin to exercise until 1831: "Governmental functions are not to be regarded as non-existent because they are held in abeyance or because they lie dormant for a time. If they be by their nature governmental, they are nonetheless so because use of them has had a recent beginning."

In 1941 only 5.1% of all government expenditures was for "general administrative, legislative and judicial" pur-

[1] *South Carolina* v. *United States*, 199 U. S. 437, 456 (1905); *Helvering* v. *Gerhardt*, 304 U. S. 405, 417 (1938).

[2] See *Commissioner* v. *Ten Eyck*, 76 F. (2d) 515 (1935).

poses.[1] These actual expenditures by American government, federal, state and local, show how far we have come in the evolution of our thinking about what government ought to do. We doubt if it ever was the general feeling that government should provide no more than a legislative, a judiciary and a chief executive. But if that concept of government was ever acceptable to Americans, it has long since vanished.

The Bureau of the Census classifies general-government expenditures into eighteen categories. In this listing, the combined "general administrative, legislative and judicial" expenditures of all American governments ranked eighth. It was exceeded by (1) Protection (military, police, fire, inspection), (2) Welfare (relief, public assistance and institutional), (3) Schools, (4) Transportation (highways and waterways), (5) Social insurance (old age and unemployment), (6) Interest and (7) Natural resources (agriculture, forests, reclamation, floods). These seven fields of government activity accounted for 82.6% of total expenditures. To complete the range of governmental activities in order of size of expenditures, we have: (8) General administrative, legislative and judicial, (9) Debt retirement, (10) Hospitals, (11) Sanitation, (12) Contributions to public service enterprises, (13) Pensions, (14) Miscellaneous, (15) Recreation, (16) Health, (17) Correction and (18) Libraries.

Even though public libraries were hardly known in 1789, the federal tax collector of 1945 would have a hard time convincing the American people today that libraries are outside the "usual" or "traditional" province of local government. Our evolving concept of that province has added many such new methods of fulfilling the original democratic "governmental function" of promoting the public welfare.

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[1] "Financing Federal, State, and Local Governments: 1941," *supra*, Table 16.

That primary function of government remains; only the methods of meeting the basic need change with changing *mores*.

A similar commentary may be made regarding the group of adjectival tests which are gauged to the preservation of some undefined measure of state government. The phrases in this category are "strictly governmental," "essential governmental" and "indispensable governmental" functions. Sometimes the theme is embroidered by speaking of functions "which the State can only do itself."[1] A number of such phrases appear in *Helvering v. Gerhardt*[2] which speaks of the functions of the States "essential to their continued existence," "essential to the maintenance of a State government" and functions "without which the State could not continue to exist as a governmental entity."

The first question must be whether the States are to be preserved as effective and independent instrumentalities of local government or whether they are to be preserved as merely historical vestiges. The question is whether they are to exercise their governmental powers in new ways to meet changing conditions or whether the requirement that they must continue to exist is satisfied if they remain only different colored patches on a map.

In one sense, no function is indispensable to the continued existence of some form of state government. Few, if any, of the most precious powers of American government have not, at one time or another in history, been regularly exercised by private persons and corporations. The collection of taxes has been spoken of as an essential governmental activity. Yet, farming of the taxes to private individuals was once a common practice.[3] War was

[1] *Flint v. Stone Tracy Co.*, 220 U. S. 107, 172 (1911).
[2] 304 U. S. 405 (1938).
[3] Encyclopedia Britannica, vol. 6, p. 904; vol. 9, p. 90.

commonly carried on between the city-states in Renaissance Italy by contracting with a condottiere who hired his soldiers from Switzerland or some of the German States.[1] Parcel post is a relatively new venture for the federal government[2] and one which it still shares with private express companies.

History shows that there is no governmental power which has not been delegated to private persons. Huge portions of this country were administered in colonial times by private corporations, chartered by the Crown but exercising every governmental power within the area under their control. The Massachusetts Bay Company was one of these. The Dutch West India Company settled and provided the law for what is now New York. Even individuals received such delegation of powers. Sir James Carteret was the proprietor of and sole law in a great portion of what is now New Jersey. William Penn was proprietor and lawmaker of the present Commonwealth of Pennsylvania. In Canada, the Hudson Bay Company was the law and the only law in a vast region. The entire Empire of India was governed by the British East India Company even within the last hundred years. The Dutch East India Company governed the East Indies.

It seems that, in a literal sense, there is no function which only the State can do itself. The test of "essentiality" in a literal sense being valueless, the question of what is a proper function of state government becomes a choice of what Mr. Justice BLACK called "individual philosophies."[3] And if that path is followed, the Court will continue to be faced with a procession of these cases in which

[1] *Id.*, vol. 6, p. 223.

[2] Unknown before 1879 when it was permitted for packages weighing less than four pounds. The present scope of the federal parcel post was established only in 1912. See Encyclopedia Britannica, vol. 18, p. 316.

[3] Concurring in *Helvering* v. *Gerhardt*, 304 U. S. 405, 426 (1938).

it will be called upon to decide political problems which it has been traditionally loathe to consider.

Yet there is an interpretation of the "essential" type of adjectival test which eliminates the difficulty. We do not see how it can be disputed that the most essential of a democratic state's possible functions is the promotion of the public welfare. In that sense and in that sense only it can quite properly be said that state immunity may be restricted to essential activities of state government. It can hardly be that the "essential" type of test was intended merely to preserve the machinery of state government—the mere skeleton of the legislature, executive and judiciary, on which at the present time only 5.1% of government revenues are expended.[1] In a democracy the machinery exists merely to provide for the welfare of the people. It follows that if a State, in order to promote the public welfare, determines to perform an activity directly rather than to regulate it, it is doing so in the exercise of that power to promote the general welfare which is the most indispensable and essentially governmental of all the powers necessary to its existence.

Of course in construing this type of test, as in the companion type which talks of "traditional" and "usual" "governmental functions," we must not be tied in any narrow sense to the conception of any past generation as to what is indispensable to effective state government. Government, whether federal or state, must meet the needs of the people as they appear at the present time, or they do not earn the right to survive. Again we point out that the reconciling factor is that in democratic governments of all times, the difference has been only on means but never on the broad principle of the state's power and duty to act in a way which the people feel is best adapted to the solu-

[1] "Financing Federal, State and Local Governments: 1941," *supra*, Table 16.

tion of their problems and the problem of their well-being. That was the view of 1789; it is the view today.

There is no problem in determining whether in fact the primary motive for the performance of the activity was to give a public service or to fill a public need. The presumption is that the State has acted for that purpose. The Court already has at hand an armory of methods to determine whether state regulatory legislation is reasonable when challenged under the due process clause of the Fourteenth Amendment. The record of public agitation for an activity, the debates in the state or local legislature, the reports of fact-finding commissions and of legislative committees and sub-committees and legislative declarations of emergency and necessity may all be considered.

2. Precedent and the True Test.

It remains for us to consider the objection that the line of demarcation between immune and taxable state activities, property and income which we advance may violate the precedents stemming from *South Carolina* v. *United States*, 199 U. S. 437 (1905). It might be sufficient to answer in Mr. Justice CARDOZO's language that the *mores* of 1905 are not those of today. The majority justices in that case considered the possibility of the acquisition and management of public utilities like gas and water. They were so distressed by the prospect that they were impelled to ask rhetorically: "Would the state, by taking into possession these public utilities lose its republican form of government?"[1]

Yet when the Court in *Brush* v. *Commissioner*, 300 U. S. 352 (1937), classified the operation of municipal water works as an "essential governmental function," it no longer seemed troubled by a fear that it was thereby destroying the republican form of state government. The federal

[1] 199 U. S. 437, 451 (1905).

government has both preceded and followed the way of municipalities in providing power without any strong feeling that the foundation of the republic was being undermined.

But aside from changing *mores* the question as to what is the effective precedent in this field is most puzzling. The actual holdings are few and quite evenly balanced. We have pronouncements that lending money to a private railway is governmental and immune[1] but that rehabilitation of a private railway is not.[2] We have decisions that the sale of alcoholic beverages is a taxable private business,[3] but that the sale of potable water is an immune public service.[4] And we have the view that charging admission to a college football game is a taxable activity.[5]

Much can be said for the argument that there is no sound distinction between providing a direct service to promote the public good and providing a service in order to make money, which in turn would be used in support of the public good; that in reason both should be immune. Particularly is this so in the light of the rule so recently put forward that federal immunity is co-extensive with federal constitutional powers. The application of this doctrine to the States would leave no state activity taxable on the basis of precedent alone.

The rule of federal immunity as we are taught by *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95, 102 (1941), is:

> "The federal government is one of delegated powers, and from that it necessarily follows that any

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[1] *United States* v. *Baltimore & Ohio Railroad Co.*, 17 Wall. 322 (1873).

[2] *Helvering* v. *Powers*, 293 U. S. 214 (1934).

[3] *South Carolina* v. *United States*, 199 U. S. 437 (1905); *Ohio* v. *Helvering*, 292 U. S. 360 (1934).

[4] *Brush* v. *Commissioner*, 300 U. S. 352 (1937).

[5] *Allen* v. *Regents*, 304 U. S. 439 (1938).

constitutional exercise of its delegated powers is governmental."

We have tried to complete the syllogism implied in this sentence. The key seems to be in some assumed difference, unexpressed, between delegated powers and reserved powers. Yet the mere fact of delegation is not a difference which has any relation to "governmentality." Perhaps the thought is that the federal government has not been delegated any powers except those appropriate to the exercise of such admittedly "governmental" powers as the regulation of interstate and foreign commerce, the power to make war and foreign treaties. If an activity of the federal government is constitutional at all, it is because it is an appropriate exercise of those governmental powers. Applying this logic to the States, we seem led to the conclusion that when a state activity is undertaken as an appropriate exercise of a state power to promote the public welfare, the activity is within the scope of the immunity.

In the federal cases the effort is not to determine whether there is something intrinsically "governmental" or "commercial" in the activity of mortgage loans[1] or in the operation of railroads and steamship lines.[2] The question is solely whether the activity is an appropriate exercise of some express delegated powers, like the regulation of interstate commerce, all of which are governmental in the federal sphere.

In the case of the States, it seems that a like inquiry is indicated. The power to take all steps consistent with the Federal Constitution to promote the general welfare and improve the health, safety and morals of its people is perhaps the highest governmental power and duty of the States. If a state activity is an appropriate exercise of

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[1] *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95 (1941).

[2] *New York ex rel. Rogers* v. *Graves*, 299 U. S. 401 (1937).

that power, either by regulation or by actual operation; it seems that the lesson of the federal cases requires that the activity be considered immune even though surplus revenues may be incidentally produced.

Reason would be offended by a ruling that power generation by the Tennessee Valley Authority is an immune function of government while power generation by the Department of Water and Power of the City of Los Angeles is a taxable function of government if both are undertaken to provide a needed public service. Reason would not accept a ruling that the federal participation in the Colorado River Compact is an immune activity of government while the participation of the States which joined in the Compact is something else. The federal government has not gone beyond the powers granted by the founding fathers, but the means it has used in the activities it has undertaken to carry out those powers go far beyond the wildest possible dreams of the most imaginative men of 1789. The reconciliation seems to be in the purpose of the undertaking and not in the manner of its effectuation for both the States and the federal government.

If this analysis is not sound, then the statement in the *Bismarck Lumber Co.* case that the federal government's activities are governmental because they are delegated, is a complete *non sequitur.* It is equally proper to say that all state activities are immune because they are reserved in the Constitution.

Our analysis is consonant with more decisions than it offends. The scope of state immunity was first outlined in a dictum in *Veazie Bank* v. *Fenno,* 8 Wall. 533, 547 (1869). It was there stated to apply to "all necessary agencies for legitimate purposes of State government."

The first case actually involving the question of the "governmentality" of state functions was *United States* v. *Baltimore & Ohio R. R. Co.,* 17 Wall. 322 (1873). The

City of Baltimore had lent $5,000,000 to the Baltimore & Ohio Railroad in return for a mortgage on the railroad property, at a specified rate of interest, in order to encourage the building of the railroad with Baltimore as a terminus. The United States attempted to collect a tax on the interest paid on this mortgage to the City of Baltimore. The Court held that the tax was on the City's income and not on the railroad company. The United States Attorney General then argued that the transaction was not strictly governmental and therefore not within the immunity doctrine. He cited a provision in the 1866 Taxing Act which said: "Provided that it is the intent hereby to exempt from liability to taxation such state, county, town or other municipal corporation, in the exercise only of functions strictly belonging to them in their ordinary governmental and municipal capacity."

The Court did not waste time in comparing the transaction with the ordinary operations of investment banking. It pointed out that the action by the City was "with a view to its commercial prosperity," that it was "exercised for the benefit of the community, that is, in the course of its municipal business or duties," that it was "acting in its capacity of an agent of the state, delegated to exercise certain powers for the benefit of the municipality called the City of Baltimore." The Court decided that the transaction was "within the range of the municipal duties of the City" and that whether it should have been undertaken "was a question for the decision of the City • • • to be decided solely with reference to public and municipal interests • • • not a question to be here discussed."

Quite obviously we have here, in the initial state case on the question, a decision that a State's immunity is as broad as its powers to undertake an activity "in the public interest." *Cf.* 12 Ops. Atty. Gen. (U. S.) 277 (1867).

The question was not raised again until *South Carolina* v. *United States*, 199 U. S. 437 (1905). Much language in

the opinion is not consistent with the rule already established in the *Baltimore & Ohio* case, but portions of the opinion make it clear that the Court was not at all convinced that South Carolina had "gone into the liquor business" for the primary purpose of regulating the traffic to improve public health or welfare. The Court said (199 U. S. 437, 454):

> "The profits from the business in the year 1901, as appears from the findings of fact were over half a million dollars. Mingling the thought of profit with the necessity of regulation may induce the state to take possession, in like manner, of tobacco, oleomargarine, and all other objects of internal revenue tax. If one state finds it thus profitable, other states may follow * * *."

Even the Court in *United States* v. *Baltimore & Ohio R. R. Co.* might have held the liquor dispensary system taxable if it had been convinced, as the Court in the *South Carolina* case apparently was, that the primary purpose of the activity was not the improvement of the public health or welfare. In this sense, the *South Carolina* case, like the Georgia football case of *Allen* v. *Regents*, 304 U. S. 489 (1938), is perfectly consistent with the line of demarcation which we advocate if there is to be any line, and which we have drawn from the *Baltimore & Ohio Railroad* case, from *Brush* v. *Commissioner*, 300 U. S. 352 (1937), and from *Pittman* v. *Home Owners' Loan Corp.*, 308 U. S. 21 (1939), and *Federal Land Bank* v. *Bismarck Lumber Co.*, 314 U. S. 95 (1941).

Ohio v. *Helvering*, 292 U. S. 360 (1934), was obviously a case where the Court considered itself bound by the *South Carolina* case. The Court did not have the advantage of a full argument of the issue on the merits. The decision was made on a motion by the State of Ohio for leave to file a bill of complaint invoking the original jurisdiction of this Court. The motion was denied on the ground that

the question was foreclosed on its merits. Perhaps, if the Court had consented to hear argument by the State of Ohio and the fuller briefing which would have occurred if jurisdiction had actually been taken, the State might have been able to convince the Court that its operation of the liquor dispensary system in Ohio in 1934 was primarily to promote the public welfare and not for the purpose of profit as the Court appears to have believed it was in the case of South Carolina in 1905.

The next decision on the nature of a "governmental function" was *Helvering* v. *Powers*, 293 U. S. 214 (1934). Frankly, the language in the case cannot be reconciled with the decision in *United States* v. *Baltimore & Ohio R. R. Co.* and the rule which we have derived from that and the later cases. The Court said that even if the State was permanently operating the Boston Street Railway for reasons which it considered in the best interests of the public, the activity would nevertheless be taxable. But the facts of the case were hardly such as to make the claim for immunity very appealing.

In the first place, the case involved a tax not on the State or a municipality or other agency, but on the salary of a so-called "public officer." As it subsequently developed in *Helvering* v. *Gerhardt*, 304 U. S. 405 (1938), and in *Graves* v. *New York ex rel. O'Keefe*, 306 U. S. 466 (1939), the Court was already at the point where the immunity of state or federal salaries seemed like an overextension of the immunity of either sovereign. In the second place, the so-called "public officer" in the *Powers* case was the trustee of a private corporation in receivership, whose salary was a charge on the private corporation's receipts. In the third place, the State was merely seeking to rehabilitate a private corporation. The State's status was closely akin to that of the federal government when, through the appointment of trustees by a bankruptcy court, it "assumes the operation" of a private business.

The last case in which this Court classified a state activity which was undertaken to promote the public health and welfare was *Brush* v. *Commissioner*, 300 U. S. 352 (1937). And in that case there was a complete return to the original principles of *United States* v. *Baltimore & Ohio R. R. Co.* and a tacit if not actual reversal of the dicta in *South Carolina* v. *United States*, 199 U. S. 437 (1905), and *Helvering* v. *Powers*, 293 U. S. 214 (1934). In the *Brush* case this Court held that the operation of a municipal waterworks is "an essential governmental function" and immune from federal taxation. None of the Justices disagreed with the holding that the activity was an "essential governmental function." Justices STONE and CARDOZO concurred on the ground that the applicable Treasury regulation provided for exemption to public employees engaged in the exercise of an "essential governmental function." Although they were not convinced that the Constitution required the immunity of Mr. Brush's salary, they accepted the decision that the activity in question was an "essential governmental function" within the meaning of the regulation.

The opinion showed that the City had taken over the activity in 1831 because it had become dissatisfied with the private control. The history of the government operation was shown to have resulted from the "public interest." Stress was placed on "the governmental power to deal with water" and that the service was necessary for "the health and comfort of the City's population." It was clearly inconsistent with the *South Carolina* case since the *South Carolina* case pointed to municipal water service as a public utility activity which was not a governmental function,[1] and the *Brush* case held to the contrary. The *South Carolina* case drew support from the analogy of the "governmental versus proprietary" distinction in the field of

[1] 199 U. S. 437, 454 (1905).

municipal tort liability;[1] the *Brush* case rejected the analogy outright.[2]

The *Brush* case gave many citations to show that water had generally been a matter of public concern. But the nub of the case is contained in the following principle (300 U. S. 353, 371):

> "It may be, as it is suggested, that private corporations would be able and willing to undertake to provide a supply of water for all purposes; but if the State and City of New York be of opinion, as they evidently are, that the service should not be entrusted to private hands but should be rendered by the City itself as an appropriate means of discharging its duty to protect the health, safety and lives of its inhabitants, we do not doubt that it may do so in the exercise of its essential governmental functions."

Here we have the true rule, the minimum rule of immunity to which the States subscribe. It is a holding, not

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[1] 199 U. S. 437, 461 (1905).

[2] 300 U. S. 352, 363 (1937). The following articles criticize the distinction between "proprietary" and "governmental" functions even in the tort field from which it was imported into the field of intergovernmental immunity: "Distinction between Government and Proprietary Functions of Municipal Corporations," Delmar W. Dobbridge, 23 Mich. Law Review, 325 (1925); "The Extension of Municipal Liability in Tort," Charles W. Tooke, 19 Va. Law Review, 97 (1932); "State and Municipal Liability in Tort—Proposed Statutory Reform," Edwin M. Borchard, 20 Amer. Bar Assn. Journal, 747 (1934); "Tort Liability of Municipal Corporations in Indiana," Alma Chattin, 10 Ind. Law Journal 329 (1935); "Government Liability in Tort," Edwin M. Borchard, 34 Yale Law Journal 1, 129, 229; 35 Yale Law Journal 1, 757, 1039; 28 Columbia Law Review 734 (1924); "The Foundations of the Distinction Between Public and Private Functions in Respect to the Common Law Tort Liability of Municipal Corporations," James D. Barrett, 16 Oregon Law Review 250 (1937); "Municipal Tort Liability in Operation," Edgar Fuller and A. James Casner, 54 Harvard Law Review 437 (1941); "Governmental Responsibility for Torts in Minnesota," Orville C. Peterson, 26 Minnesota Law Review, 293, 480, 613, 700, 854 (1942); Thurston, "Government Proprietary Corporations" (1942), preface page 2.

a dictum. It is the answer to the argument that precedent requires that the State's immunity need be any narrower than the State's power to adopt any appropriate means of effectuating its power and duty of promoting the general welfare of its people, protecting their lives and morals and preserving their health and safety.

If the Court feels compelled by precedent to distinguish between different types of state activities, there seems no possible alternative to the test we have suggested. It is democratic because it leaves to the people of the States the decisions as to the scope of the States' activities, and saves the Court from deciding the political question of the propriety of state activities. It is an expedient rule—it should end the plaguing recurrence of case after case to decide on "traditional" or "essential" character. It is fair as between States and the federal government because it applies the same test for immunity in both cases. It avoids stagnancy in state government by permitting the people of the States to decide with changes in times and conditions what changed approach they will have to their problems. It involves no affront to sovereignty because it forbids federal taxation of the States in all cases where they act, as sovereigns, to promote the public good. It preserves the place of the States in the federal system since it prevents federal control and regulation by selective or conditioned exemption designed to substitute the policy of the federal government for the policy of the local governments in purely local spheres. It protects the fiscal balance between the States and the federal government by preventing a huge new burden of taxation of the States. It avoids curtailing local governmental services because of the new tax burden. It leaves intact the state policy of using the system of paying for the cost of some services by charges on the users rather than on the general taxpayers. It avoids widespread municipal bankruptcy which would be caused by taxes on state and municipal revenues

which have already been pledged or ear-marked for the retirement of revenue or general obligations. It fits the precedents more closely than any other test.

In the light of the now proven and theretofore undreamed of capacity of the federal government to expand its revenues without any embarrassment from state activities, the rule which we have proposed could not possibly threaten any impairment of the federal taxing powers. On the contrary, the public work of the States and Cities and their contribution to the welfare and prosperity of the American people vastly increases the revenue potential of the federal government.

In short, "We have a principle which is safe for the states, and safe for the Union. We are relieved, as we ought to be, from clashing sovereignty; from interfering powers; from a repugnancy between a right in one government to pull down what there is an acknowledged right in another to build up; from the incompatibility of a right in one government to destroy what there is a right in another to preserve."[1]

POINT IV

The extent to which a State may withdraw property or income or activities from the reach of federal taxation by enlarging its property ownership or its activities.

Point I of this brief is responsive to the Court's first question. As indicated, that question admits only a negative answer.

The answer to the Court's second question is implicit in Points II and III, which have been devoted primarily

[1] *M'Culloch* v. *Maryland*, 4 Wheat. 316, 403 (1819).

to intergovernmental taxation and immunity. In Point II we concluded that intergovernmental taxation is constitutional only if actually necessary to preserve the existence of the taxing government, and that such necessity does not in fact exist. Although this appears to be the soundest rule, nevertheless some line of division between types of state activities has been suggested in prior decisions of this Court. The Court has spoken of the difference between "governmental" functions, and "business" or "commercial" activities of a State. It has qualified the phrase "governmental function" with adjectives such as "usual," "traditional," "essential" and "indispensable." If for some reason it is felt necessary to discriminate between types of state activities, the true purpose of these qualifications supplies the minimum possible answer to the Court's second question:—A state may enlarge its property ownership and activities without becoming subject to the Congressional taxing power at least so long as it is rendering a service which its people believe "should be rendered by the city (or State) itself as an appropriate means of discharging its duty to protect the health, safety and lives of its inhabitants." See *Brush* v. *Commissioner*, 300 U. S. 352, 371 (1937) and cases therein cited.

Conclusion

In submitting this brief, we, the National Association of Attorneys General, and the individual Attorneys General whose names are subscribed hereto, sincerely trust that we are in truth acting as friends of this Court. It is our firm conviction that the problem of intergovernmental taxation and immunity is one of pressing importance directly affecting the maintenance of sound relationships between the state and federal governments. We would fail in our duty as public officers, as members of the Bar and as citizens, if we did not seek to aid in its solution.

The rules which we urge and the principles which we advocate represent our collective judgment as to what constitutes sound constitutional law and sound public policy. While as state officers we have emphasized the place of the States in our federal system, we do not urge our views upon the Court in any narrow spirit of partisan advocacy. We do so in a sincere belief that they are in the best interests, not only of the States and the Nation, but also of our citizens to promote whose welfare both the States and the Nation exist.

Dated: December 1, 1945.

Respectfully submitted,

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Supreme Court of the United States

OCTOBER TERM, 1945

NO. 5.

STATE OF NEW YORK AND SARATOGA SPRINGS COMMISSION AND SARATOGA SPRINGS AUTHORITY, Petitioners,

v.

UNITED STATES OF AMERICA.

BRIEF ON REARGUMENT, FOR THE COMMONWEALTH OF PENNSYLVANIA AS AMICUS CURIAE.

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UNITED STATES OF AMERICA.

BRIEF ON REARGUMENT, FOR THE COMMONWEALTH OF PENNSYLVANIA AS AMICUS CURIAE.

The Attorney General for the Commonwealth of Pennsylvania has joined in the "Brief for the States as *Amici Curiae*".

This additional brief is prompted by the emphasis placed by counsel upon such decisions as *South Carolina v. United States*, 199 U. S. 437 (1905), and *Ohio v. Helvering*, 292 U. S. 360 (1934).

The Pennsylvania Liquor Control Board was created by Act of November 29, 1933 (Pamphlet Laws, page 36, Title 47, Purdon's Penna. Stats., sec. 744). The purpose of the Act was to provide a system of control for the sale of intoxicating liquors, which was made

necessary by the impending repeal of the Eighteenth Amendment to the Federal Constituton.

The Liquor Control Board has been paying the excise tax on liquor sold. This court has raised an additional question as to the power of the federal government to tax the income of a state from an activity.

The title of this Act was

> "An Act To regulate and restrain the sale, importation, and use of certain alcoholic beverages; conferring powers and imposing duties upon the Pennsylvania Liquor Control Board, the Department of Public Instruction, other officers of the State government, courts, and district attorneys; authorizing the establishment and operation of State stores for the sale of such beverages not for consumption on the premises; forbidding importation of bringing of such beverages into the State except as herein provided; prohibiting certain sales or practices in, connection with, and transactions in such beverages by licensees and others; making disposition of the receipts from State stores and of license fees; and imposing penalties."

The purpose of the Act was declared in Section 3 as follows:

> "This act shall be deemed an exercise of the police power of the Commonwealth for the protection of the public welare, health, peace and morals of the people of the Commonwealth, and to prohibit forever the open saloon; * * *"

Section 801, prescribing the effective date of the Act, enacted "* * * nothing herein contained shall authorize the sale of any liquor prior to the day when

the Twenty-first Amendment to the Constitution of the United States is ratified by conventions in at least three-fourths of the several states, * * *

The effect of the Act was to require that all liquor sold in Pennsylvania must pass through the hands of the Pennsylvania Liquor Control Board. Regular tests in the laboratory of the Board protect the public from liquor containing poisonous or other injurious ingredients. Liquor could be sold only in pursuance of a license for specified premises operated by a hotel, restaurant or club. (Sec. 401) Saloons were abolished. Each of these provisions was clearly within the scope of police power.

Prior to the Act of November 29, 1933, P. L. 36, the Commonwealth of Pennsylvania had never enacted any legislation providing for the sale by the State of intoxicating liquor. Amendment XXI, repealing the Prohibition Amendment, was proposed by Congress on February 20, 1933 and was declared ratified on December 15, 1933. The Commonwealth was compelled to pick up the problem of liquor control where the Federal Government left off. It was decided not to go back to the old ~~prohibition~~ liquor law which was in force in Pennsylvania prior to the Eighteenth Amendment. Conditions had changed. The Commonwealth was compelled to deal with a new situation created by Federal prohibition in which powerful organizations engaged in illegal sale of liquor were operating through the country. The Commonwealth endeavored to solve this problem by a system of control which outlawed all sales of liquor which did not pass through the hands of the Liquor Control Board.

The purpose of the Pennsylvania Liquor Control Law was not to obtain revenue by making a profit on the sale of liquor. It did not seek to interfere with any revenue which the Federal Government was collecting, for the reason that the Federal Prohibition Law had prohibited the sale of liquor and virtually terminated such revenue.

The purpose of the Liquor Control Law, we repeat, was not to obtain revenue, but was enacted by the Commonwealth as the most effective measure of solving a problem which devolved upon it when Federal control was abandoned.

The Liquor Control Law was an innovation in Pennsylvania, but public approval is evidenced by the continuance of the law in force.

The Pennsylvania Liquor Control Board is an agency clearly undertaken to "promote the public health, safety and welfare, and not for the purpose of making money." (Brief for the States, pp. 4, 66, 71).

The Pennsylvania Liquor Control Board is therefore, performing a paramount "public service". It is not merely engaged in selling liquors as appears to be the view taken of the South Carolina and Ohio Agencies in the brief for the State of New York (p. 44).

These considerations were relied upon in the opinions in such cases as *South Carolina v. United States*, 199 U. S. 437 and *Ohio v. Helvering*, 292 U. S. 360;

(1) Any allowance of immunity to a state agency is at the expense of the sovereign power of the nation to tax.

It is argued that if the states should concur in expanding their activities into new fields formerly occupied by private business, the power of the national government to raise revenue would be largely crippled.

The forty years which have elapsed since the ruling in the *South Carolina case* have not confirmed this apprehension. On the other hand the Federal government has engaged in many new activities and created new agencies which were unheard of when the Constitution was adopted and did not exist even at the time of the South Carolina decision. Loans amounting to billions of dollars have been made by such agencies as the Reconstruction Finance Corporation, Home Owners' Loan Corporation and the Federal Loan Bank. Such loans are free from state taxation and an enormous amount of state tax has been displaced thereby. Postal savings and government loans have withdrawn vast sums from checking and savings deposits in private banks which were taxable by the states and have absorbed other sums which would have otherwise found investment in securities taxable by the state.

Social Security and War Risk Insurance have accumulated large amounts of money which might otherwise have been invested in policies of private insurance companies, the income and investments of which would be taxed by the states. Federal Employment service, Parcel Post and other activities absorb business taxable by a state.

In contrast with the amount of state taxes which have been displaced by the tremendous growth of Federal activities, the increase in immunities of state

agencies from Federal taxation seems almost inconsiderable.

The constitution apparently affords no protection to the states against encroachments by such truly gigantic agencies of the Federal government. Since the adoption of the Federal constitution, economic changes have wrought a tremendous expansion of interstate commerce. When the constitution was adopted, business was local. Now it is largely national. Business activities which were formerly intra-state and local, have become interstate and nationwide. The great human wants, such as food, clothing, fuel, amusements, building materials, transportation, which were once furnished from local sources, are now supplied through the channels of interstate commerce. The result of this transition has been to exempt from state taxation much business which was formerly taxable by the states. Although a business becomes interstate, it is still dependant upon the police powers of the states for protection. This the federal government does not afford.

At the beginning of this nation taxes were principally levied upon land. This source of taxation for the states was protected by the provision that direct taxes by the Federal Government must be apportioned according to population and that was rarely done. Taxation of real and personal property by the national government is still so restricted, but income from real and personal property has increased prodigiously, and Federal taxes have been increased thereby.

(2) The people of all the states are represented in Congress and through that representation they may exercise control over the taxing power of the United States.

This control, we submit, is theoretical rather than actual. Are the citizens of the United States able to prevent through their representatives in Congress the passage of a Federal law taxing so-called "proprietary" enterprises of a state?

In the first place such a Federal law would affect the various states unequally. Citizens of states in which there were few large municipalities or centers of population would seldom enjoy the benefits of such proprietary agencies, and would have no interest in voting against such a measure. The people of a state which did not own any oil wells or mineral springs would not be solicitous in safeguarding the income of a state which did have the same. Some states enjoy little or no income and depend entirely upon taxation for revenue.

Even if Congress proposed a general excise tax which would affect all states equally, would the people be able to defeat it through their representatives in Congress? To do so, they would have to select candidates who would stand for such agencies only, and ignore today such vital issues as the continuance of the Selective Service Law, compulsory military training, a broader Social Security Law, full federal employment, and many other issues which absorb the interest of the people of this nation tody.

Many millions of voters favor the maintenance of high federal taxes in order to make possible such benefits as Social Security, full employment benefits, old age pensions, unemployment compensation and general relief. Other millions do not pay or do not knowingly pay any income or other federal taxes.

In this interplay of issues, how would a citizen vote so as to prevent the taxation of the mineral springs of

New York or the Liquor Control Board of Pennsylvania? His representative in Congress may be depended upon to resist in some degree federal taxation infringing upon income of a state. Participation in the government at Washington, however, tends to make the official nationally minded and interested in increasing the revenues of the Federal government.

(3) The distinction between public and private or governmental and proprietary functions.

This distinction was originally contrived by the courts to avoid exemption from liability for negligence of public employees. It is, we submit, unsound in principle and results in many inconsistencies. The authorities hold that a state or municipality may levy taxes and exercise the power of eminent domain for purpose of constructing a water supply system or an artificial gas plant, etc. Both of these powers are restricted to public purposes.

Respectfully submitted,

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No. 5.

STATE OF NEW YORK and SARATOGA SPRINGS COMMISSION and SARATOGA SPRINGS AUTHORITY

Petitioners,

vs.

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BRIEF OF THE STATE OF ILLINOIS AS AMICUS CURIAE.

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UNITED STATES OF AMERICA.

BRIEF OF THE STATE OF ILLINOIS AS AMICUS CURIAE.

FOREWORD.

The Attorney General of Illinois has been privileged to read the brief of other state Attorneys General. He adopts unqualifiedly and earnestly joins in the arguments which it presses upon this court. It would be a work of subarrogation to repeat the substance of that excellent exposition of the principles which it contains.

But in view of the very great importance of the first question which the court has propounded, the Attorney Gen-

eral deems it his duty briefly to suggest certain considerations that are not touched upon in the briefs thus far filed. These additional considerations, which are respectfully submitted in this brief, are simple in character and need not be elaborately argued. Their force can, it is believed, be appreciated as soon as their substance is perceived.

ARGUMENT.

I.

The historicity not only of constitutional principles but of preconstitutional doctrine is opposed to any tax levied directly upon states in their sovereign character, even apart from any decisions of this court.

Briefs already filed in this case address the practical considerations implied by a federal tax upon state sovereignties. They demonstrate the extent to which federal policy of taxation must directly control state government. They all urge, so that repetition of the point in this brief is not necessary, the theoretical repugnancy implicit in the concept of a tax by one sovereign upon another.

But the other briefs do not, in our view, give proper emphasis and accent to the argument that, although the Constitution of the United States was intended to be a plastic document, adequate to the exigencies of an unforeseeable future, certain political doctrines were so universally the creed and faith of its framers that they must be held to abide within every phrase of its text; and one of these tenets had to do specifically with restriction upon federal power of taxation.

It must be recalled that the odium of capital levies, whether called taxes or otherwise, by governments whose

seats were remote from the people had played a vitally important part both in the American Revolution and in the framing of the Articles of Confederation. Indeed, so fearful were the citizens (who had so recently been only colonial subjects) of federal tyranny through the guise of federal taxes that the original Confederation was rendered virtually impotent because no federal taxing powers were provided.

It can hardly be supposed that those who framed and those who adopted and confirmed the original Constitution of the United States intended to cede to the newly born Union any powers in that Union to tax directly the states which had created it.

The argument is most forcibly put in this wise: What can we reasonably conjecture would have been the result had the founders of the Constitution, at the time that it was proposed to the states for original ratification, told the people and their representatives that it authorized the laying of taxes directly and without fixed limits upon state capitol buildings, state arsenals, state roads and canals—in short, upon all of the wealth of the states? This court knows that the Constitution would never have even been written, much less ratified, with any such clause in its terms.

Yet a direct property tax, of the kind that the Constitution authorizes with respect to citizens, can be levied upon all of these instruments of sovereignty if the first question asked by the court in this case be answered in the affirmative.

Now, if it be supposed, as it must be supposed, that a constitution portending such a result would never have been ratified, then the immunity of the States (provided, of course, that they do not engage in non-sovereign activities, competitive with private sources of national taxation) must be held to be as plainly a constitutional provision as

though it had been explicitly uttered in the text of the Constitution.

We cannot forbear emphasis of the fact that "it is a constitution that we are expounding." Even if it could be supposed that sound fiscal policy required the taxation of the states (and we unequivocally reject any such supposition), authority for it would have to be found in the organic law of the country.

We submit that no sanction for such taxation can be found in the Constitution.

II.

The federal government cannot visit federal duties upon state officials, if such duties must be performed on behalf of the state as a sovereign in its sovereign and not in its corporate character.

The other briefs filed do not advert to the capital principle, which has not been questioned since its first enunciation, that *the federal government may not compel state officers to act in their official capacity with respect to the federal government, even when they are under a duty to act.*

Nothing is clearer, for example, than that it is the duty of a governor of a state to render to another state a fugitive from such latter state. Nevertheless, in *Kentucky* v. *Dennison,* 65 U. S. 66, this court held that its writ of *mandamus* would not lie to compel a governor to perform that duty. The court said, at page 107, that

> "the Federal Government, under the Constitution, **has no power to impose on a State officer, as such, any duty whatever, and compel him to perform it;** * * * "

the court further observing that if such power existed, its exercise "might impose on him duties of a character in-

compatible with the rank and dignity to which he was elevated by the State."

The court, speaking even more plainly, said at page 108, although

> "Congress may authorize a particular State officer to perform a particular duty; but if he declines to do so, it does not follow that he may be coerced or punished for his refusal."

Now, if state officers cannot be compelled to perform on behalf of their states any duties whatever by the federal government, then they cannot be compelled to file tax returns or disburse the public funds in payment of federal taxes.

Doubtless this rule yields to an apparent exception where the state acts as a mere corporate proprietor of a non-governmental enterprise. But in such cases, the acts of its officers are not sovereign in their quality.

We urge this latter consideration because it has been inadvertently ignored in the briefs heretofore filed in this case. Nevertheless, it affords an insuperable objection to an affirmative answer to the question asked by the court.

CONCLUSION.

For the reasons urged in the briefs filed by the State of New York, as well as those filed by other *amici curiae*, for the reasons urged in this brief, we respectfully submit that the question asked by the court should be answered in the negative.

Respectfully submitted,

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8 Q. 14-8

SUPREME COURT OF THE UNITED STATES.

No. 5.—October Term, 1945.

State of New York and Saratoga Springs Commission and Saratoga Springs Authority, Petitioners,
vs.
The United States of America.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[January 14, 1946.]

Mr. Justice Frankfurter announced the judgment of the Court and delivered an opinion in which Mr. Justice Rutledge joined.

Section 615(a)(5) of the 1932 Revenue Act, 47 Stat. 169, 264, imposed a tax on mineral waters.[1] The United States brought this suit to recover taxes assessed against the State of New York on the sale of mineral waters taken from Saratoga Springs, New York.[2] The State claims immunity from this tax on the ground that "in the bottling and sale of the said waters the defendant State of New York was engaged in the exercise of a usual, traditional and essential governmental function". The claim was

[1] "Sec. 615. Tax on Soft Drinks.
(a) There is hereby imposed . . .
(5) Upon all natural or artificial mineral waters or table waters, whether carbonated or not, and all imitations thereof, sold by the producer, bottler, or importer thereof, in bottles or other closed containers, at over 12½ cents per gallon, a tax of 2 cents per gallon."

[2] The history of New York's relations to the springs at Saratoga may be briefly summarized. Under previous private operation the flow of the springs had been substantially diminished by excessive pumping. In 1911 the State of New York began to acquire title to all the lands on which the mineral springs were located at Saratoga Springs. In order to conserve the springs for beneficial operation, the State took various measures until, in 1930, control over the springs in the State Reservation was given to the newly-created Saratoga Springs Commission. In 1933, the Commission leased the 'springs' facilities and delegated their management to the Saratoga Springs Authority, a public benefit corporation of New York.
During the years 1932 to 1934, for which the tax is asserted, the Commission and the Authority operated the Reservation as a health resort and spa. There are recreation facilities, bath houses, drink halls, a research laboratory, and other buildings on the grounds. Some of the mineral waters of the springs that have a medicinal value are bottled and sold to distributors, retailers, and directly to consumers. The sales are promoted by advertising and customarily yield a profit which is applied to meeting in part the expenses of operating the other facilities. The remainder of those expenses is met by annual legislative appropriations.

rejected by the District Court and judgment went for the United States. 48 F. Supp. 15. The judgment was affirmed by the Circuit Court of Appeals for the Second Circuit. 140 F. (2d) 608. The strong urging of New York for further clarification of the amenability of States to the taxing power of the United States led us to grant certiorari. 322 U. S. 724.

On the basis of authority the case is quickly disposed of. When States sought to control the liquor traffic by going into the liquor business, they were denied immunity from federal taxes upon the liquor business. *South Carolina* v. *United States*, 199 U. S. 437; *Ohio* v. *Helvering*, 292 U. S. 360. And in rejecting a claim of immunity from federal taxation when Massachusetts took over the street railways of Boston, this Court a decade ago said: "We see no reason for putting the operation of a street railway [by a State] in a different category from the sale of liquors." *Helvering* v. *Powers*, 293 U. S. 214, 227. We certainly see no reason for putting soft drinks in a different constitutional category from hard drinks. See also *Allen* v. *Regents*, 304 U. S. 439.

One of the greatest sources of strength of our law is that it adjudicates concrete cases and does not pronounce principles in the abstract. But there comes a time when even the process of empiric adjudication calls for a more rational disposition than that the immediate case is not different from preceding cases. The argument pressed by New York and the forty-five other States who, as *amici curiae*, have joined her deserves an answer.

Enactments levying taxes made in pursuance of the Constitution are, as other laws are, "the supreme Law of the Land". Art. VI, Constitution of the United States; *Flint* v. *Stone Tracy Co.*, 220 U. S. 108, 153. The first of the powers conferred upon Congress is the power "To lay and collect Taxes, Duties, Imposts and Excises . . . ", Art. I, § 8. By its terms the Constitution has placed only one limitation upon this power, other than limitations upon methods of laying taxes not here relevant: Congress can lay no tax "on articles exported from any State." Art. I, § 9. Barring only exports, the power of Congress to tax "reaches every subject." *License Tax Cases*, 5 Wall. 462, 471. But the fact that ours is a federal constitutional system, as expressly recognized in the Tenth Amendment, carries with it implications regarding the taxing power as in other aspects of government. See, *e. g.*, *Hopkins Savings Ass'n* v. *Cleary*, 296 U. S. 315. Thus, for Congress to tax State activities while leaving untaxed the same activi-

ties pursued by private persons would do violence to the presuppositions derived from the fact that we are a Nation composed of States.

But the fear that one government may cripple or obstruct the operations of the other early led to the assumption that there was a reciprocal immunity of the instrumentalities of each from taxation by the other. It was assumed that there was an equivalence in the implications of taxation by a State of the governmental activities of the National Government and the taxation by the National Government of State instrumentalities. This assumed equivalence was nourished by the phrase of Chief Justice Marshall that "the power to tax involves the power to destroy". *McCulloch* v. *Maryland*, 4 Wheat. 316, 431. To be sure, it was uttered in connection with a tax of Maryland which plainly discriminated against the use by the United States of the Bank of the United States as one of its instruments. What he said may not have been irrelevant in its setting. But Chief Justice Marshall spoke at a time when social complexities did not so clearly reveal as now the practical limitations of a rhetorical absolute. See Holmes, J., in *Long* v. *Rockwood*, 277 U. S. 142, 148, and in *Panhandle Oil Co.* v. *Mississippi*, 277 U. S. 218, 223. The phrase was seized upon as the basis of a broad doctrine of intergovernmental immunity, while at the same time an expansive scope was given to what were deemed to be "instrumentalities of government" for purposes of tax immunity. As a result, immunity was until recently accorded to all officers of one government from taxation by the other, and it was further assumed that the economic burden of a tax on any interest derived from a government imposes a burden on that government so as to involve an interference by the taxing government with the functioning of the other government. See *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514; *Helvering* v. *Producers Corp.*, 303 U. S. 376; *Graves* v. *N. Y. ex rel. O'Keefe*, 306 U. S. 466, 480-81.

To press a juristic principle designed for the practical affairs of government to abstract extremes is neither sound logic nor good sense. And this Court is under no duty to make law less than sound logic and good sense. When this Court for the first time relieved State officers from a non-discriminatory Congressional tax, not because of anything said in the Constitution but because of the supposed implications of our federal system, Mr. Justice Bradley pointed out the invalidity of the notion of reciprocal

intergovernmental immunity. The considerations bearing upon taxation by the States of activities or agencies of the federal government are not correlative with the considerations bearing upon federal taxation of State agencies or activities. The federal government is the government of all the States, and all the States share in the legislative process by which a tax of general applicability is laid. "The taxation by the State governments of the instruments employed by the general government in the exercise of its powers," said Mr. Justice Bradley, "is a very different thing. Such taxation involves an interference with the powers of a government in which other States and their citizens are equally interested with the State which imposes the taxation."[3] Since then we have moved away from the theoretical assumption that the National Government is burdened if its functionaries, like other citizens, pay for the upkeep of their State governments, and we have denied the implied constitutional

[3] The views of Mr. Justice Bradley have been so vindicated by time and experience that his whole compact opinion deserves to be recalled:

"I dissent from the opinion of the court in this case, because, it seems to me that the general government has the same power of taxing the income of officers of the State governments as it has of taxing that of its own officers. It is the common government of all alike; and every citizen is presumed to trust his own government in the matter of taxation. No man ceases to be a citizen of the United States by being an officer under the State government. I cannot accede to the doctrine that the general government is to be regarded as in any sense foreign or antagonistic to the State governments, their officers, or people; nor can I agree that a presumption can be admitted that the general government will act in a manner hostile to the existence or functions of the State governments, which are constituent parts of the system or body politic forming the basis on which the general government is founded. The taxation by the State governments of the instruments employed by the general government in the exercise of its powers, is a very different thing. Such taxation involves an interference with the powers of a government in which other States and their citizens are equally interested with the State which imposes the taxation. In my judgment, the limitation of the power of taxation in the general government, which the present decision establishes, will be found very difficult of control. Where are we to stop in enumerating the functions of the State governments which will be interfered with by Federal taxation? If a State incorporates a railroad to carry out its purposes of internal government, or a bank to aid its financial arrangements, reserving, perhaps, a percentage on the stock or profits, for the supply of its own treasury, will the bonds or stock of such an institution be free from Federal taxation? How can we now tell what the effect of this decision will be? I cannot but regard it as founded on a fallacy, and that it will lead to mischievous consequences. I am as much opposed as any one can be to any interference by the general government with the just powers of the State governments. But no concession of any of the just powers of the general government can easily be recalled. I, therefore, consider it my duty to at least record my dissent when such concession appears to be made. An extended discussion of the subject would answer no useful purpose." *Collector* v. *Day*, 11 Wall. 113, 128-29.

immunity of federal officials from State taxes. *Graves* v. *N. Y.* ex rel. *O'Keefe, supra.* See *Gillespie* v. *Oklahoma,* 257 U. S. 501, criticized in *Burnet* v. *Colorado Oil & Gas Co.,* 285 U. S. 393, 401, and explicitly overruled in *Helvering* v. *Producers Corp.,* 303 U. S. 376; *Long* v. *Lockwood,* 277 U. S. 142, overruled in *Fox Film Corp.* v. *Doyal,* 286 U. S. 123; *Collector* v. *Day,* 11 Wall. 113, and *New York* ex rel. *Rogers* v. *Graves,* 299 U. S. 401, overruled in *Graves* v. *N. Y.* ex rel. *O'Keefe, supra.*

In the meantime, cases came here, as we have already noted, in which States claimed immunity from a federal tax imposed generally on enterprises in which the State itself was also engaged. This problem did not arise before the present century, partly because State trading did not actively emerge until relatively recently, and partly because of the narrow scope of federal taxation. In *South Carolina* v. *United States,* 199 U. S. 437, immunity from a federal tax on a dispensary system, whereby South Carolina monopolized the sale of intoxicating liquors, was denied by drawing a line between taxation of the historically recognized governmental functions of a State, and business engaged in by a State of a kind which theretofore had been pursued by private enterprise. The power of the federal government thus to tax a liquor business conducted by the State was derived from an appeal to the Constitution "in the light of conditions surrounding at the time of its adoption." *South Carolina* v. *United States, supra,* at 457. That there is a Constitutional line between the State as government and the State as trader, was still more recently made the basis of a decision sustaining a liquor tax against Ohio. "If a state chooses to go into the business of buying and selling commodities, its right to do so may be conceded so far as the Federal Constitution is concerned; but the exercise of the right is not the performance of a governmental function . . . . When a state enters the market place seeking customers it divests itself of its *quasi* sovereignty *pro tanto,* and takes on the character of a trader, so far, at least, as the taxing power of the federal government is concerned." *Ohio* v. *Helvering, supra* at 369. When the *Ohio* case was decided it was too late in the day not to recognize the vast extension of the sphere of government, both State and national, compared with that with which the Fathers were familiar. It could hardly remain a satisfactory constitntional doctrine that only such State activities are immune from federal taxation as were engaged in by the States in 1787. Such a static concept of government denies its essential

nature. "The science of government is the most abstruse of all sciences; if, indeed, that can be called a science which has but few fixed principles, and practically consists in little more than the exercise of a sound discretion, applied to the exigencies of the state as they arise. It is the science of experiment." *Anderson* v. *Dunn*, 6 Wheat. 204, 226.

When this Court came to sustain the federal taxing power upon a transportation system operated by a State, it did so in ways familiar in developing the law from precedent to precedent. It edged away from reliance on a sharp distinction between the "governmental" and the "trading" activities of a State, by denying immunity from federal taxation to a State when it "is undertaking a business enterprise of a sort that is normally within the reach of the federal taxing power and is distinct from the usual governmental functions that are immune from federal taxation in order to safeguard the necessary independence of the State." *Helvering* v. *Powers*, *supra* at 227. But this likewise does not furnish a satisfactory guide for dealing with such a practical problem as the constitutional power of the United States over State activities. To rest the federal taxing power on what is "normally" conducted by private enterprise in contradiction to the "usual" governmental functions is too shifting a basis for determining constitutional power and too entangled in expediency to serve as a dependable legal criterion. The essential nature of the problem cannot be hidden by an attempt to separate manifestations of indivisible governmental powers. See Wambaugh, *Present Scope of Government* (1897) 20 A. B. A. Rep. 307; Frankfurter, *The Public and its Government* (1930).

The present case illustrates the sterility of such an attempt.[4] New York urges that in the use it is making of Saratoga Springs it is engaged in the disposition of its natural resources. And so it is. But in doing so it is engaged in an enterprise in which the State sells mineral waters in competition with private waters, the sale of which Congress has found necessary to tap as a source of revenue for carrying on the National Government. To say that the States cannot be taxed for enterprises generally pursued, like the sale of mineral water, because it is somewhat connected with a State's conservation policy, is to invoke an irrelevance to the fed-

[4] This method of solving a problem inherent in a federal constitutional system has been found equally inconclusive in Latin America. See Amadeo, Argentine Constitutional Law (1943) 97-103.

eral taxing power. Liquor control by a State certainly concerns the most important of a State's natural resources—the health and well-being of its people. See *Mugler* v. *Kansas*, 123 U. S. 623, 662; *Crane* v. *Campbell*, 245 U. S. 304, 307. If in its wisdom a State engages in the liquor business and may be taxed by Congress as others engaged in the liquor business are taxed, so also Congress may tax the States when they go into the business of bottling water as others in the mineral water business are taxed even though a State's sale of its mineral waters has relation to its conservation policy.

In the older cases, the emphasis was on immunity from taxation. The whole tendency of recent cases reveals a shift in emphasis to that of limitation upon immunity. They also indicate an awareness of the limited rôle of courts in assessing the relative weight of the factors upon which immunity is based. Any implied limitation upon the supremacy of the federal power to levy a tax like that now before us, in the absence of discrimination against State activities, brings fiscal and political factors into play. The problem cannot escape issues that do not lend themselves to judgment by criteria and methods of reasoning that are within the professional training and special competence of judges. Indeed the claim of implied immunity by States from federal taxation raises questions not wholly unlike provisions of the Constitution, such as that of Art. IV, § 4, guaranteeing States a republican form of government, see *Pac. States Tel. & T. Co.* v. *Oregon*, 223 U. S. 118, which this Court has deemed not within its duty to adjudicate.

We have already held that by engaging in the railroad business a State cannot withdraw the railroad from the power of the federal government to regulate commerce. *United States* v. *California*, 297 U. S. 175. See also *University of Illinois* v. *United States*, 289 U. S. 48. Surely the power of Congress to lay taxes has impliedly no less a reach than the power of Congress to regulate commerce. There are, of course, State activities and State-owned property that partake of uniqueness from the point of view of intergovernmental relations. These inherently constitute a class by themselves. Only a State can own a Statehouse; only a State can get income by taxing. These could not be included for purposes of federal taxation in any abstract category of taxpayers

without taxing the State as a State. But so long as Congress generally taps a source of revenue by whomsoever earned and not uniquely capable of being earned only by a State, the Constitution of the United States does not forbid it merely because its incidence falls also on a State. If Congress desires, it may of course leave untaxed enterprises pursued by States for the public good while it taxes like enterprises organized for private ends. Cf. *Springfield Gas Co.* v. *Springfield*, 257 U. S. 66; *University of Illinois* v. *United States*, *supra*, at 57; *Puget Sound Co.* v. *Seattle*, 291 U. S. 619. If Congress makes no such differentiation and, as in this case, taxes all vendors of mineral water alike, whether State vendors or private vendors, it simply says, in effect, to a State: "You may carry out your own notions of social policy in engaging in what is called business, but you must pay your share in having a nation which enables you to pursue your policy." After all, the representatives of all the States, having, as the appearance of the Attorneys General of forty-six States at the bar of this Court shows, common interests, alone can pass such a taxing measure and they alone in their wisdom can grant or withhold immunity from federal taxation of such State activities.

The process of Constitutional adjudication does not thrive on conjuring up horrible possibilities that never happen in the real world and devising doctrines sufficiently comprehensive in detail to cover the remotest contingency. Nor need we go beyond what is required for a reasoned disposition of the kind of controversy now before the Court. The restriction upon States not to make laws that discriminate against interstate commerce is a vital constitutional principle, even though "discrimination" is not a code of specifics but a continuous process of application. So we decide enough when we reject limitations upon the taxing power of Congress derived from such untenable criteria as "proprietary" against "governmental" activities of the States, or historically sanctioned activities of Government, or activities conducted merely for profit,[5]

[5] Attempts along similar lines to solve kindred problems arising under the Canadian and Australian Constitutions have also proved a barren process. See Pond, Intergovernmental Immunity: A Comparative Study of the Federal System (1941) 26 Iowa L. Rev. 272; Kennedy & Wells, The Law of the Taxing Power in Canada (1931) 35-37.

Even where the Constitution of a federal system explicitly deals with the problem of intergovernmental taxation, as in Brazil, litigation is not escaped

Australia Constitution Act, 1900, § 114, in Edgerton, Federations and Unions in the British Empire (2d ed., 1924) 225;

and find no restriction upon Congress to include the States in levying a tax exacted equally from private persons upon the same subject matter.

Judgment affirmed.

Mr. Justice JACKSON took no part in the consideration or decision of this case.

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and nice distinctions have to be made. See cases arising under Article 10 of the Constitution of 1891 and under Article 32 of the Constitution of 1937: Appelação civel, No. 2.884, 13 Rivesta do Supremo Tribunal 203 (1917); Appelação civel, No. 2.900, 14 Revista do Supreme Tribunal 44 (1918); Appelação civel, No. 2.536, 19 Revista do Suprema Tribunal 76 (1919); Recuso de mandado de segurança No. 617, 56 Archivo Judiciario 3 (1940); Agravo de petição, No. 8.024, 59 Archivo Judiciario 85 (1941). Article 32 of the Constitution of 1937, the present Brazilian Constitution, provides: "The Union, the States, and the Municipalities are forbidden: . . . *a*) to tax goods, income, or services of each other." Speaking of the earlier Constitution, a commentator notes: "These limitations on the federal taxing power are all taken from our own jurisprudence, either by direct transcription from the Constitution of the United States or by the incorporation of principles laid down in decisions of our [the United States] supreme court, as is the case with the last named prohibition"—"the prohibition against taxing property, revenues, or services of the States." James, Federal Basis of the Brazilian System (1923) 45.

Mr. Justice RUTLEDGE, concurring.

I join in the opinion of Mr. Justice FRANKFURTER and in the result. I have no doubt upon the question of power. The shift from immunity to taxability has gone too far, and with too much reason to sustain it, as respects both state functionaries and state functions, for backtracking to doctrines founded in philosophies of sovereignty more current and perhaps more realistic in an earlier day. Too much is, or may be, at stake for the nation to permit relieving the states of their duty to support it, financially as otherwise, when they take over increasingly the things men have been accustomed to carry on as private, and therefore taxable, enterprise. Competitive considerations unite with the necessity for securing the federal revenue, in a time when the federal burden grows heavier proportionately than that of the states, to forbid that they be free to undermine rather than obligated to sustain the nation's financial requirements.

All agree that not all of the former immunity is gone. For the present I assent to the limitation against discrimination, which I take to mean that state functions may not be singled out for taxation when others performing them are not taxed or

for special burdens when they are. What would happen if the state should take over a monopoly of traditionally private, income-producing business may be left for the future, in so far as this has not been settled by *South Carolina* v. *United States*, 199 U. S. 437. Perhaps there are other limitations also, apart from the practical one imposed by the state's representation in Congress. If the way were open, I would add a further restricting factor, not of constitutional import, but of construction.

With the passing of the former broad immunity, I should think two considerations well might be taken to require that, before a federal tax can be applied to activities carried on directly by the states, the intention of Congress to tax them should be stated expressly and not drawn merely from general wording of the statute applicable ordinarily to private sources of revenue. One of these is simply a reflection of the old immunity, in the presence of which, of course, it would be inconceivable that general wording, such as the statute now in question contains, could be taken as intended to apply to the states.[1] The other is that, quite apart from reflections of that immunity, I should expect that Congress would say so explicitly, were its purpose actually to include state functions, where the legal incidence of the tax falls upon the state.[2] And the concurring opinion of Mr. Justice Bradley in *United States* v. *Baltimore & Ohio R. R. Co.*, 17 Wall. 322, 333, indicates that he may have been of this general view.

Nevertheless, since *South Carolina* v. *United States, supra*, such a rule of construction seems not to have been thought required.[3] Accordingly, although I gravely doubt that when Congress taxed every "person" it intended also to tax every state, the ruling has been made[4] and I therefore acquiesce in this case.

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[1] The drive, removal of the immunity the effect of inverting the intention of Congress, in its later use of the same formula, is a leap in construction longer than seems reasonable to make.

[2] Cf. 26 U. S. C. § 22(a) where Congress has specifically provided that compensation for personal service, includible in gross income, includes compensation for personal service as an officer or employee of a state, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing.

[3] University of Illinois *v.* United States, 289 U. S. 48; Ohio *v.* Helvering, 292 U. S. 360. See Manhattan Co. *v.* Blake, 148 U. S. 412. In Graves *v.* New York *ex rel.* O'Keefe, 306 U. S. 466, 479, 480, the Court said, in another connection: "It is true that the silence of Congress, when it has authority to speak, may sometimes give rise to an implication as to the Congressional purpose. . . . But there is little scope for the application of that doctrine to the tax immunity of governmental instrumentalities."

[4] See Ohio *v.* Helvering, *supra*.

Mr. Chief Justice STONE concurring.

Mr. Justice REED, Mr. Justice MURPHY, Mr. Justice BURTON and I concur in the result. We are of the opinion that the tax here involved should be sustained and the judgment below affirmed.

In view of our decisions in *South Carolina* v. *United States*, 199 U. S. 437, *Ohio* v. *Helvering*, 292 U. S. 360, *Helvering* v. *Powers*, 293 U. S. 214, and *Allen* v. *Regents*, 304 U. S. 439, we would find it difficult not to sustain the tax in this case, even though we regard as untenable the distinction between "governmental" and "proprietary" interests on which those cases rest to some extent. But we are not prepared to say that the national government may constitutionally lay a non-discriminatory tax on every class of property and activities of States and individuals alike.

Concededly a federal tax discriminating against a State would be an unconstitutional exertion of power over a coexisting sovereignty within the same framework of government. But our difficulty with the formula, now first suggested as offering a new solution for an old problem, is that a federal tax which is not discriminatory as to the subject matter may nevertheless so affect the State, merely because it is a State that is being taxed, as to interfere unduly with the State's performance of its sovereign functions of government. The counterpart of such undue interference has been recognized since Marshall's day as the implied immunity of each of the dual sovereignties of our constitutional system from taxation by the other. *McCulloch* v. *Maryland*, 4 Wheat. 316. We add nothing to this formula by saying, in a new form of words, that a tax which Congress applies generally to the property and activities of private citizens may not be in some instances constitutionally extended to the States, merely because the States are included among those who pay taxes on a like subject of taxation.

If the phrase "non-discriminatory tax" is to be taken in its long accepted meaning as referring to a tax laid on a like subject matter, without regard to the personality of the taxpayer, whether a State, a corporation or a private individual, it is plain that there may be non-discriminatory taxes which, when laid on a State, would nevertheless impair the sovereign status of the State quite as much as a like tax imposed by a State on property or activities of the national government. *Mayo* v. *United States*, 319 U. S. 441, 447-448. This is not because the tax can be regarded

as discriminatory but because a sovereign government is the taxpayer, and the tax, even though non-discriminatory, may be regarded as infringing its sovereignty.

A State may, like a private individual, own real property and receive income. But in view of our former decisions we could hardly say that a general non-discriminatory real estate tax (apportioned), or an income tax laid upon citizens and States alike could be constitutionally applied to the State's capitol, its State-house, its public school houses, public parks, or its revenues from taxes or school lands, even though all real property and all income of the citizen is taxed. If it be said that private citizens do not own State-houses or public school buildings or receive tax revenues, it may equally be said that private citizens do not conduct a State-owned liquor business or derive revenue from a State-owned athletic field. Obviously Congress, in taxing property or income generally, is not taxing a State "as a State" because the State happens to own real estate or receive income. Whether a State or an individual is taxed, in each instance the taxable occasion is the same. The tax reaches the State because of the Congressional purpose to lay the tax on the subject matter chosen, regardless of who pays it. To say that the tax fails because the State happens to be the taxpayer is only to say that the State, to some extent undefined, is constitutionally immune from federal taxation. Only when and because the subject of taxation is State property or a State activity must we consider whether such a non-discriminatory tax unduly interferes with the performance of the State's functions of government. If it does, then the fact that the tax is non-discriminatory does not save it. If we are to treat as invalid, because discriminatory, a tax on "State activities and State-owned property that partake of uniqueness from the point of view of intergovernmental relations", it is plain that the invalidity is due wholly to the fact that it is a State which is being taxed so as unduly to infringe, in some manner, the performance of its functions as a government which the Constitution recognizes as sovereign.

It is enough for present purposes that the immunity of the State from federal taxation would, in this case, accomplish a withdrawal from the taxing power of the nation a subject of taxation of a nature which has been traditionally within that power from the beginning. Its exercise now, by a non-discriminatory tax,

does not curtail the business of the state government more than it does the like business of the citizen. It gives merely an accustomed and reasonable scope to the federal taxing power. Such a withdrawal from a non-discriminatory federal tax, and one which does not bear on the State any differently than on the citizen, is itself an impairment of the taxing power of the national government, and the activity taxed is such that its taxation does not unduly impair the State's functions of government. The nature of the tax immunity requires that it be so construed as to allow to each government reasonable scope for its taxing power, *Metcalf & Eddy* v. *Mitchell*, 269 U. S. 514, 524. The national taxing power would be unduly curtailed if the State, by extending its activities, could withdraw from it subjects of taxation traditionally within it. *Helvering* v. *Powers, supra*, 225; *Ohio* v. *Helvering, supra*; *South Carolina* v. *United States, supra*, and see *Murray* v. *Wilson Distilling Co.*, 213 U. S. 151, 173, explaining *South Carolina* v. *United States, supra.*

The problem is not one to be solved by a formula, but we may look to the structure of the Constitution as our guide to decision. "In a broad sense, the taxing power of either government, even when exercised in a manner admittedly necessary and proper, unavoidably has some effect upon the other. The burden of federal taxation necessarily sets an economic limit to the practical operation of the taxing power of the states, and *vice versa.* Taxation by either the state or the federal government affects in some measure the cost of operation of the other.

"But neither government may destroy the other nor curtail in any substantial manner the exercise of its powers. Hence the limitation upon the taxing power of each, so far as it affects the other, must receive a practical construction which permits both to function with the minimum of interference each with the other; and that limitation cannot be so varied or extended as seriously to impair either the taxing power of the government imposing the tax . . . or the appropriate exercise of the functions of the government affected by it." *Metcalf & Eddy* v. *Mitchell, supra*, 523-524.

Since all taxes must be laid by general, that is, workable, rules, the effect of the immunity on the national taxing power is to be determined not quantitatively but by its operation and tendency in withdrawing taxable property or activities from the reach of

federal taxation. Not the extent to which a particular State engages in the activity, but the nature and extent of the activity by whomsoever performed is the relevant consideration.

Regarded in this light we cannot say that the Constitution either requires ~~or permits~~ immunity of the State's mineral water business from federal taxation, or denies to the federal government power to lay the tax.

Mr. Justice DOUGLAS, with whom Mr. Justice BLACK concurs, dissenting.

I.

If *South Carolina* v. *United States*, 199 U. S. 437, is to stand, the present judgment would have to be affirmed. For I agree that there is no essential difference between a federal tax on South Carolina's liquor business and a federal tax on New York's mineral water business. Whether *South Carolina* v. *United States* reaches the right result is another matter.

Mr. Justice Brandeis stated that "*Stare decisis* is usually the wise policy, because in most matters it is more important that the applicable rule of law be settled than that it be settled right." *Burnet* v. *Coronado Oil & Gas Co.*, 285 U. S. 393, 406. But throughout the history of the Court *stare decisis* has had only a limited application in the field of constitutional law. And it is a wise policy which largely restricts it to those areas of the law where correction can be had by legislation. Otherwise the Constitution loses the flexibility necessary if it is to serve the needs of successive generations.

I do not believe *South Carolina* v. *United States* states the correct rule. A State's project is as much a legitimate governmental activity whether it is traditional, or akin to private enterprise, or conducted for profit. Cf. *Helvering* v. *Gerhardt*, 304 U. S. 405, 426-427. A State may deem it as essential to its economy that it own and operate a railroad, a mill, or an irrigation system as it does to own and operate bridges, street lights, or a sewage disposal plant. What might have been viewed in an earlier day as an improvident or even dangerous extension of state activities may today be deemed indispensable. But as Mr. Justice White said in his dissent in *South Carolina* v. *United States*, any activity in which a State engages within the limits of its police power is

a legitimate governmental activity. Here a State is disposing of some of its natural resources. Tomorrow it may issue securities, sell power from its public power project, or manufacture fertilizer. Each is an exercise of its power of sovereignty. Must it pay the federal government for the privilege of exercising that inherent power? If the Constitution grants it immunity from a tax on the issuance of securities, on what grounds can it be forced to pay a tax when it sells power or disposes of other natural resources?

II.

One view, just announced, purports to reject the distinction which *South Carolina* v. *United States* drew between those activities of a State which are and those which are not strictly governmental, usual, or traditional. But it is said that a federal tax on a State will be sustained so long as Congress "does not attempt to tax a State because it is a State." Yet if that means that a federal real estate tax of general application (apportioned) would be valid if applied to a power dam owned by a state but invalid if applied to a state-house, the old doctrine has merely been poured into a new container. If, on the other hand, any federal tax on any state activity were sustained unless it discriminated against the State, then a constitutional rule would be fashioned which would undermine the sovereignty of the States as it has been understood throughout our history. Any such change should be accomplished only by constitutional amendment. The doctrine of state immunity is too intricately involved in projects which have been launched to be whittled down by judicial fiat.

III.

Woodrow Wilson stated the starting point for me when he said[1] that

> "the States of course possess every power that government has ever anywhere exercised, except only those powers which their own constitutions or the Constitution of the United States explicitly or by plain inference withhold. They are the ordinary governments of the country; the federal government is its instrument only for particular purposes."

The Supremacy Clause, Article VI, clause 2, applies to federal laws within the powers delegated to Congress by the States. But it is antagonistic to the very implications of our federal system

[1] Constitutional Government in the United States (1908), pp. 183-184.

to say that the power of Congress to lay and collect taxes, Article I, § 8, includes the power to tax any state activity or function so long as the tax does not discriminate against the States.[2] As stated in *United States* v. *Railroad Co.*, 17 Wall. 322, 327-328,

> "The right of the States to administer their own affairs through their legislative, executive, and judicial departments, in their own manner through their own agencies, is conceded by the uniform decisions of this court and by the practice of the Federal government from its organization. This carries with it an exemption of those agencies and instruments, from the taxing power of the Federal government. If they may be taxed lightly, they may be taxed heavily; if justly, oppressively. Their operation may be impeded and may be destroyed, if any interference is permitted."

Can it be that a general federal tax on the issuance of securities would be constitutional if applied to the issuance of municipal securities or of state bonds or of the securities of public utility districts organized by the States? Could the States be classified with farmers, business men, industrial workers, judges, and other ordinary citizens and required to pay an income tax to the federal government? It is said that a federal income tax on the tax revenues of a State would not be sustained because such a tax would interfere with a sovereign function of the State. But can it be that a federal income tax on state revenues derived not from taxes but from the sale of mineral water, liquor, lumber and the like, would be sustained?

A tax is a powerful, regulatory instrument. Local government in this free land does not exist for itself. The fact that local government may enter the domain of private enterprise and operate a project for profit does not put it in the class of private business enterprise for tax purposes. Local government exists to provide for the welfare of its people, not for a limited group of stockholders. If the federal government can place the local governments on its tax collector's list, their capacity to serve the needs

[2] As stated in United States v. California, 297 U. S. 175, 184, 185, the immunity of state instrumentalities from federal taxation "is implied from the nature of our federal system and the relationship within it of state and national governments, and is equally a restriction on taxation by either of the instrumentalities of the other." It went on to say in justification of making state activities subject to the exercise by Congress of the commerce power, "But there is no such limitation upon the plenary power to regulate commerce. The state can no more deny the power if its exercise has been authorized by Congress than can an individual."

of their citizens is at once hampered or curtailed. The field of federal excise taxation alone is practically without limits. Many state activities are in marginal enterprises where private capital refuses to venture. Add to the cost of these projects a federal tax and the social program may be destroyed before it can be launched. In any case, the repercussions of such a fundamental change on the credit of the States and on their programs to take care of the needy and to build for the future would be considerable. To say the present tax will be sustained because it does not impair the State's functions of government is to conclude either that the sale by the State of its mineral water is not a function of government or that the present tax is so slight as to be no burden. The former obviously is not true. The latter overlooks the fact that the power to tax lightly is the power to tax severely. The power to tax is indeed one of the most effective forms of regulation. And no more powerful instrument for centralization of government could be devised. For with the federal government immune and the States subject to tax, the economic ability of the federal government to expand its activities at the expense of the States is at once apparent. That is the result whether the rule of *South Carolina* v. *United States* be perpetuated or a new rule of discrimination be adopted.

The notion that the sovereign position of the States must find its protection in the will of a transient majority of Congress is foreign to and a negation of our constitutional system. There will often be vital regional interests represented by no majority in Congress. The Constitution was designed to keep the balance between the States and the nation outside the field of legislative controversy.

The immunity of the States from federal taxation is no less clear because it is implied. The States on entering the Union surrendered some of their sovereignty. It was further curtailed as various Amendments were adopted. But the Tenth Amendment provides that "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." The Constitution is a compact between sovereigns. The power of one sovereign to tax another is an innovation so startling as to require explicit authority if it is to be allowed. If the power of the federal government to tax the States is conceded, the reserved power of the States

guaranteed by the Tenth Amendment does not give them the independence which they have always been assumed to have. They are relegated to a more servile status. They become subject to interference and control both in the functions which they exercise and the methods which they employ. They must pay the federal government for the privilege of exercising the powers of sovereignty guaranteed them by the Constitution,[3] whether, as here, they are disposing of their natural resources, or tomorrow they issues securities or perform any other acts within the scope of their police power.

Of course, the levying of the present tax does not curtail the business of the state government more than it does the like business of the citizen. But the same might be true in the case of many state activities which have long been assumed to be immune from federal taxation. When a municipality acquires a water system or an electric power plant and transmission facilities, it withdraws projects from the field of private enterprise. Is the tax immunity to be denied because a tax on the municipality would not curtail the municipality more than it would the prior private owner? Is the municipality to be taxed whenever it engages in an activity which once was in the field of private enterprise and therefore was once taxable? Every expansion of state activity since the adoption of the Constitution limits the reach of federal taxation if state immunity is recognized. Yet none would concede that the sovereign powers of the States were limited to those which they exercised in 1787. Nor can it be said that if the present tax is not sustained there will be withdrawn from the taxing power of the federal government a subject of taxation which has been traditionally within that power from the beginning. Not until *South Carolina v. United States* was it held that so-called business activities of a State were subject to federal taxation. That was

[3] That fact distinguishes those cases where a citizen seeks tax immunity because his income was derived from a State or the federal government. Recognition of such a claim would create a "privileged class of taxpayers" (*Helvering* v. *Gerhardt*, *supra*, p. 416) and extend the tax immunity of the States or the federal government to private citizens. It was in protest to the recognition of such a derivative immunity that Mr. Justice Bradley dissented in *Collector* v. *Day*, 11 Wall. 113, 128, where the Court held unconstitutional a federal tax on the salary of a judicial officer of a State. As Mr. Justice Bradley stated, "No man ceases to be a citizen of the United States by being an officer under the State government." 11 Wall. p. 128. And see Graves *v.* O'Keefe, 306 U. S. 466, holding that salaries of federal employees may be constitutionally included in a non-discriminatory state income tax.

after the turn of the present century. Thus the major objection to the suggested test is that it disregards the Tenth Amendment, places the sovereign States on the same plane as private citizens, and makes the sovereign States pay the federal government for the privilege of exercising the powers of sovereignty guaranteed them by the Constitution.

That this idea is hostile to the view of the Framers of the Constitution is evident from Hamilton's discussion of the taxing power of the federal government in The Federalist, Nos. 30-36 (Sesquicentennial Ed. 1937) pp. 183-224. He repeatedly stated that the taxing powers of the States and of the federal government were to be "concurrent"—"the only admissible substitute for an entire subordination, in respect to this branch of power, of the State authority to that of the Union." pp. 202-203. He also stated, "The convention thought the concurrent jurisdiction preferable to that subordination; and it is evident that it has at least the merit of reconciling an indefinite constitutional power of taxation in the Federal government with an adequate and independent power in the States to provide for their own necessities." p. 209. On such assurances could it possibly be thought that the States were so subordinate that their activities could be taxed by the federal government?

In *M'Culloch* v. *Maryland*, 4 Wheat. 316, the Court held unconstitutional a state tax on notes of the Bank of the United States. The statement of Chief Justice Marshall (pp. 429-430) is adequate to sustain the case for the reciprocal immunity of the state and federal governments:

> "If we measure the power of taxation residing in a State, by the extent of sovereignty which the people of a single State possesses, and can confer on its government, we have an intelligible standard, applicable to every case to which the power may be applied. We have a principle which leaves the power of taxing the people and property of a State unimpaired; which leaves to a State the command of all its resources, and which places beyond its reach, all those powers which are conferred by the people of the United States on the government of the Union, and all those means which are given for the purpose of carrying those powers into execution. We have a principle which is safe for the States, and safe for the Union. We are relieved, as we ought to be, from clashing sovereignty; from interfering powers; from a repugnancy between a right in one government to pull down what there is an acknowledged right in another to build up; from

the incompatibility of a right in one government to destroy what there is a right in another to preserve. We are not driven to the perplexing inquiry, so unfit for the judicial department, what degree of taxation is the legitimate use, and what degree may amount to the abuse of the power."

IV.

Those who agreed with *South Carolina* v. *United States* had the fear that an expanding program of state activity would dry up sources of federal revenues and thus cripple the national government. 199 U. S. pp. 454-455. That was in 1905.[4] That fear is expressed again today when we have the federal income tax, from which employees of the States may not claim exemption on constitutional grounds. *Helvering* v. *Gerhardt, supra.* The fear of depriving the national government of revenue if the tax immunity of the States is sustained has no more place in the present decision than the spectre of socialism, the fear of which, said Holmes "was translated into doctrines that had no proper place in the Constitution or the common law."[5]

There is no showing whatsoever that an expanding field of state activity even faintly promises to cripple the federal government in its search for needed revenues. If the truth were known, I suspect it would show that the activity of the States in the fields of housing, public power and the like have increased the level of income of the people and have raised the standards of marginal or sub-marginal groups. Such conditions affect favorably, not adversely, the tax potential of the federal government.

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[4] As the Solicitor General of New York points out, in the year when South Carolina v. United States was decided over one-fourth of the entire annual income of the federal government was derived from taxes on spirits and fermented liquors. See Annual Report, Secretary of the Treasury (1905), pp. 7, 26.

[5] Holmes, Collected Legal Papers (1921) p. 295